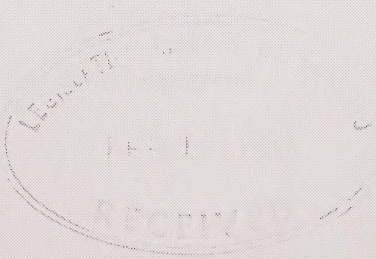

1949

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING COMMITTEE ON BANKING AND COMMERCE

To whom was referred the Bill 176, intituled: "An Act to amend The Income Tax Act and the Income War Tax Act."

THURSDAY, DECEMBER 8, 1949

ACTING CHAIRMAN

The Honourable J. G. Fogo

WITNESSES

The Honourable D. C. Abbott, P.C., M.P., Minister of Finance.

Mr. James Sinclair, M.P., Parliamentary Assistant to the Minister of Finance.

Dr. A. K. Eaton, Assistant Deputy Minister, Finance Department.

Mr. C. Gavsie, Taxation Division, National Revenue Department.

OTTAWA
EDMOND CLOUTIER, C.M.G., B.A., L.Ph.,
PRINTER TO THE KING'S MOST EXCELLENT MAJESTY
CONTROLLER OF STATIONERY
1949

ORDER OF REFERENCE

EXTRACT from the Minutes of Proceedings of the Senate of Canada, Wednesday, 7th December, 1949.

With leave,
The Senate then proceeded to the seventh Order of the Day.

Accordingly, the Honourable Senator Campbell moved that Bill (176), intituled: "An Act to amend The Income Tax Act and the Income War Tax Act" be now read a second time.

The question being put on the motion for the second reading of the Bill, it was—

Resolved in the affirmative.

The said Bill was then read the second time, and—
Referred to the Standing Committee on Banking and Commerce.

On motion, it was—
Ordered, That the Standing Committee on Banking and Commerce be authorized to print 500 copies in English and 200 copies in French of its proceedings on the Bill (176) intituled: "An Act to amend The Income Tax Act and the Income War Tax Act", and that Rule 100 be suspended in relation to the said printing.

L. C. MOYER,
Clerk of the Senate.

STANDING COMMITTEE ON BANKING AND COMMERCE

The Honourable JOHN W. DEB. FARRIS, Chairman.

The Honourable Senators Aseltine, Aylesworth, *Sir Allen*, Baird, Ballantyne, Beaubien, Bouffard, Buchanan, Burchill, Campbell, Crerar, Daigle, David, Davies, Dessureault, Duff, Euler, Fallis, Farris, Fogo, Gershaw, Gouin, Haig, Hardy, Hayden, Horner, Howard, Hugessen, Jones, King, Kinley, Lambert, Leger, MacKinnon, MacLennan, Marcotte, McGuire, McKeen, McLean, Moraud, Nicol, Paterson, Quinn, Raymond, Robertson, Roebuck, Sinclair, Taylor, Vien and Wilson—49.

THURSDAY, December 8, 1949.

Pursuant to adjournment and notice the Standing Committee on Banking and Commerce met this day at 10.30 a.m.

Present: The Honourable Senators: Beaubien, Burchill, Campbell, David, Davies, Dessureault, Euler, Fogo, Gouin, Hayden, Horner, Hugessen, Lambert, Leger, MacLennan, Marcotte, McGuire, McLean, Moraud, Nicol, Paterson, Robertson, Roebuck, Sinclair, Taylor, Vien and Wilson.—27.

In attendance: Mr. J. F. MacNeill, Law Clerk and Parliamentary Counsel.

The official reporters of the Senate.

In the absence of the Chairman and on motion of the Honourable Senator Robertson, the Honourable Senator Fogo was elected Acting Chairman.

Bill 176, "An Act to amend The Income Tax Act and the Income War Tax Act", was considered clause by clause.

The following were heard in explanation of the Bill:
The Honourable D. C. Abbott, P.C., M.P., Minister of Finance.
Dr. A. K. Eaton, Assistant Deputy Minister, Finance Department.
Mr. C. Gavsie, Taxation Division, National Revenue Department.

The Honourable Senator Nicol moved that clauses 7 and 8 of the Bill be deleted.

After discussion, the said motion was withdrawn.

At 1.15 p.m. the Committee adjourned.

At 2.00 p.m. the Committee resumed.

The following were again heard:
Dr. A. K. Eaton.
Mr. C. Gavsie.

At 3.00 p.m. the Committee adjourned.

At 4.00 p.m. the Committee resumed.

The following were heard:
Mr. James Sinclair, M.P., Parliamentary Assistant to the Minister of Finance.
Dr. A. K. Eaton.
Mr. C. Gavsie.

At 6.00 p.m. the Committee adjourned.

At 8.00 p.m. the Committee resumed.

The following were further heard:
Dr. A. K. Eaton.
Mr. C. Gavsie.

It was resolved to report the Bill without any amendment.

At 9.20 p.m. the Committee adjourned to the call of the Chairman.

Attest.

JOHN A. HINDS,
Clerk of the Committee.

MINUTES OF EVIDENCE

THE SENATE

OTTAWA, Thursday, December 8, 1949.

The Standing Committee on Banking and Commerce, to whom was referred Bill 176, an Act to amend the Income Tax Act and the Income War Tax Act, met this day at 10.30 a.m.

Hon. Mr. FOGO in the Chair.

The CHAIRMAN: Gentlemen, the business before the committee is Bill 176, an Act to amend the Income Tax Act and the Income War Tax Act; and here, from the Department of Finance, is Dr. Eaton, Assistant Deputy Minister.

Hon. Mr. VIEN: Have you got the bill that has passed the House of Commons?

The CHAIRMAN: No.

Hon. Mr. VIEN: Is it in order that we should proceed?

Hon. Mr. MORAUD: It is supposed to be distributed this morning, Senator Vien. Somebody had an advance copy last night.

Hon. Mr. ROBERTSON: There were three copies available last night, and the other ones will be available and printed by half-past eleven. I think we might proceed with Dr. Eaton indicating what the amendments were.

Hon. Mr. HAYDEN: I was wondering, if there was a general question about the effective date of the depreciation sections, should I raise that with Dr. Eaton? It does not deal with any particular section.

The CHAIRMAN: It seems to me that if you get into the effective date of depreciation you open the whole question of depreciation. It would be better to have Dr. Eaton's general remarks first, unless the committee wishes otherwise.

Hon. Mr. HAYDEN: There is a point of view with respect to the effective date that I would like to present at one stage, as to whether the effective date should be the 1st of January, 1949, or the 1st of January, 1950, and it will take me two or three minutes just to tell him why, if the committee feels that that is the way to deal with it.

The CHAIRMAN: Well, if it is agreeable to the committee you can make your remarks now.

Hon. Mr. HAYDEN: As regards making the effective date the 1st of January, 1949, it has been brought to our attention that there are many companies that issue quarterly statements, and those quarterly statements in 1949 have been issued, and there is a charge-off to depreciation in those statements according to the practice in force at the present time; that is, taking the rates and charging on the basis of original cost. These statements are issued to the public, the financial papers comment on them, investments are made, retained or disposed of on the basis of these current operating statements, and now I am told that if at the end of the year those companies have to make a statement for depreciation purposes on the basis of the new provisions, not on the basis of original cost but on that diminishing basis in relation to some of these companies, they will have to make a charge of at least 25 per cent in order to reach the amount they have written off in their three quarterly statements so far this year, and that would be impossible for them to do. That is the difficulty in making the provision

retroactive, and that is why I was suggesting or proposing to avoid confusion that an effective date of January 1, 1950, would overcome all these difficulties with companies.

Dr. EATON: Perhaps Mr. Gavsie would care to comment on that.

Mr. GAVSIE: As I understand, it would be a dollar amount of depreciation, and that consideration has been given to putting in the regulations a provision that for the year 1949 a person may take or, if he has already taken the dollar amount that he could have taken under the old system, that will be it; so there will be no hardship as to retroactiveness of this, notwithstanding anything there may be in the regulations. If a person would under the old system this year have been entitled to X dollars, the fact that under these regulations he might in this particular case get X minus 10—he would still be entitled to take X.

Hon. Mr. VIEN: But what objection is there to the 1st of January, 1950—that instead of the 1st of January, 1949, it should become effective the 1st of January, 1950?

Hon. Mr. HAYDEN: May I say that what you are in effect saying is that it would be optional in 1949 whether I take my depreciation dollarwise according to the formula now in effect or the formula presented by this bill. I can take it on either basis?

Mr. GAVSIE: Yes. The system will be in effect, but if the old basis would give them a higher dollar amount you would be entitled to take that for 1949. That would have to be in the regulations; that is what is intended in all the discussion that has taken place to date. In the bill or in the act as it exists at the present time, under section 11 (1) (*a*) there is a provision for a capital allowance to be fixed by regulation. Now that regulation has not been passed. All that is in the amending bill is the provision for what has been called so far the recapture provision, plus the definitions that go with the operational system, and in clause 8 you find the rules for the determination of capital cost; so that under the new system there will be no recapture of the normal depreciation taken up to the time of the commencement of the 1949 tax year.

Hon. Mr. HAYDEN: So if I accept the optional method you have suggested the regulations will provide, my capital value for purposes of the new method of depreciation will be the figure at the 1st of January, 1949. The amount I deduct in 1949 will be subject to recapture?

Mr. GAVSIE: That is right, but you will still get the dollar amount that you could have taken under the old regulations.

Hon. Mr. VIEN: Am I clear that the taxpayer shall have the option of either retaining the system of depreciation as it is now until the 1st of January, 1950, or else adopt the new system dollarwise, and if he does, then the year 1949 will come under this provision?

Mr. GAVSIE: No, that is not quite the case.

Hon. Mr. VIEN: I would like to have it made clear. What I have read in the press and in the *Hansard* of the Commons does not satisfy public opinion. I have heard a tremendous amount of comment and criticism with respect to the cloudy and—some have used a word I do not like to use here—the lousy way in which explanations are given out. We are ordinary common mortals, and we would like an explanation in such language as we can comprehend and then pass on to the public. Therefore I have tried to follow what has been said just now, and I must confess that, due to my own density, but there are a number of Canadians who are almost as dense as I am, I have some difficulty in understanding what is going on. I for one do not intend to allow a bill of this kind to be adopted before I understand it.

Hon. Mr. CAMPBELL: I do not feel that that is quite a fair statement to make in so far as Mr. Gavsie's explanation is concerned.

Mr. GAVSIE: I just gave an answer to Senator Hayden's question.

Hon. Mr. CAMPBELL: If I may make an attempt to explain the problem that is troubling Senator Vien, and which Mr. Gavsie has touched on very slightly, it is this, that although it will not be optional to follow the old system of depreciaion existing as it now stands on the statutes for the year 1949, the new system coming into effect as of January 1, 1949, anyone who has actually taken depreciation in a certain dollar amount on the old basis of quarterly statements or during the year will be able to write into his account that dollar figure. But the effect will be that the new basis of depreciation will commence as of January 1, 1949, so that dollar figure will be taken into consideration for the future determination of the recapture provisions in the case that the property or the asset is sold at an increased value. I think that it would be very helpful to the members of the committee if we let Mr. Gavsie explain the legislation, and I think that when he gets through we will understand it a great deal better and know how to phrase our questions.

The CHAIRMAN: I was just going to say that the very thing that I was afraid would happen has happened. We have got into a discussion of the particulars without first hearing a general explanation of the bill. It would be beneficial to us if Dr. Eaton would review the reasons for the changes, and then we could discuss the particular items and ask questions on them.

Hon. Mr. NICOL: May I ask that this particular point be brought out? Yesterday when presenting the bill our confrere, Senator Campbell, stated that it was a reduction of taxation. I personally take it that it is a very large increase of taxation, and I wish the witness in giving his explanation would tell us where this bill represents a decrease of taxation and where it represents an increase of taxation.

Dr. EATON: Perhaps I could describe the bill in this way. There are two main parts to it. First of all it provides for the decreases in taxation which were announced in the House of Commons last spring, and which were elaborated on by the Minister of Finance at that time. They were fairly extensive. To start with, the exemptions from taxation which were $750 for a single person and $1,500 for a married person, have been increased to a $1,000 for a single person and $2,000 for a married person. The increases of the allowances for dependent children and other dependents have been increased from $100 in the case of Family Allowance children, to $150 for the same class of dependent; and from $300 in the case of ordinary dependents over 16 years of age, who are not entitled to family allowances, up to $400. In addition to that the rate structure was revised downward very substantially.

Hon. Mr. HUGESSEN: On personal income?

Dr. EATON: Yes.

Hon. Mr. NICOL: In what part of the bill is that to be found?

Dr. EATON: That is in clause 10. The immediate effect of these reduced rates was given in withholding at the source. Following the announcement by the minister in the house that these changes were to be reduced, the new withholding tables were sent out to industry and there was a reduction in the amount withheld at the source comparable to the reduction in the rate structure that would be effective in 1949.

That is the main substance, if you like, of this bill. It is a bill to give effect to these reductions in personal income tax effective for 1949. So much for the individual personal income tax.

Hon. Mr. EULER: You also have the exemption of dividends on preferred shares?

Dr. EATON: That is correct. That is really part of the revised corporate tax structure, if you like. It was part of the revision of the structure as it affects corporations.

Getting into the corporate tax field, the main changes were these. The corporation income tax which was previously 30 per cent on all corporations, a flat rate of 30 per cent, was altered, and provision has been made for a reduction from what was 30 to 10 per cent on the first $10,000 of profits, and an increase from 30 to 33 per cent on profits in excess of $10,000.

Hon. Mr. NICOL: In the long run that would be an increase of taxation?

Dr. EATON: If you will allow me to complete another piece, I will give you the revenue results of all three pieces. That 10 per cent on the first $10,000 is limited in the case of related companies. Only one corporation of a group of related corporations may take the 10 per cent on the first $10,000.

Hon. Mr. EULER: Could you not split it up and say a number of corporations?

Dr. EATON: You can, but it would be of no benefit tax-wise. The reduction of 10 per cent on the first $10,000 is coupled with an increase to 33 per cent on profits in excess of $10,000. In addition to that, as part of the same re-organization, provision was made for a tax credit to individuals in respect of dividends received from Canadian corporations. That tax credit against personal income tax is measured by 10 per cent of the dividends received.

Hon. Mr. DUTREMBLAY: It is the same thing. There is 3 per cent on the 30 per cent.

Hon. Mr. HAYDEN: No. That is a different matter.

Dr. EATON: There was an increase from 30 to 33 on the corporation, but a more than corresponding relief was given to the shareholders on dividends distributed. So that if a corporation made a reasonable distribution of profits, the total amount of tax—shareholder and corporation taken together—was reduced.

The net revenue effect of these three changes which I have mentioned, a reduction on the first $10,000, an increase on profits in excess of $10,000, and the relief to persons receiving dividends cancels out, that is the cost of them to the revenue balances with the additional receipts.

Hon. Mr. EULER: The bigger company loses as the result of the increase, whereas the individual shareholder gains, and that gain is greater than what the company loses.

Dr. EATON: I would not admit the tax burden has been increased, having regard to the shareholder of the big corporation.

Hon. Mr. EULER: That is what I say, it is offset by the shareholder getting the additional credit.

Dr. EATON: Yes.

Hon. Mr. MORAUD: Is the department getting more or less revenue that way?

Dr. EATON: There is no difference. As near as we have been able to figure it out, these changes balance out.

Those are the main changes of substance in the burden of taxation. The bulk of this bill is made up of technical changes. You all know that the new income tax was completely rewritten, and the new law came into effect January 1, 1949. That was quite a job, rewriting the whole of that law. Now in this one year of operation, if you like, we continued working on the law and found in many cases there had been changes which were not intended, and it just took nine months for those changes to be brought to light. What we have done here is to have continued the study of the law and we have made quite a number of technical changes. It is the last year in which we could make changes effective on the

coming into force of this new law. For that reason you will find a lot of changes that take up quite a bit of space on paper, but which are quite technical and which do not affect very much the general burden of taxation.

I think that is about all I can say about this bill in general terms. That is the reason why it is so bulky. We have used this as a last opportunity to try and get the legislation in good shape, and the comments from outside have been useful in pointing out minor defects in the law, or places where we have unintentionally changed the tax burden through rewriting the law. These are taken care of and to date we have made all the technical changes we could discover ourselves or which have been pointed out to us from outside sources. Mr. Chairman, I think that is all I have to say at the moment.

The CHAIRMAN: Would you not say a word in general explanation of this new formula for the treatment of depreciation? If I remember correctly, the new act effective in 1949 changed the general basis of depreciation, which was formerly a matter of such depreciation only as the minister might allow, to provide that depreciation would be allowed in accordance with the regulations.

Dr. EATON: That is right.

The CHAIRMAN: I understand that this bill introduces either a new formula or supplementary material to section 11, which new formula or supplementary material ties in with proposed regulations and introduces some quite new thinking as applicable to depreciation and also introduces to a large extent, if not altogether, in a new fashion, the principle of recapture. Would you give us a general idea why this new scheme is introduced?

Dr. EATON: Yes, sir. I propose asking Mr. Gavsie to perform that task for you, sir, but I will make a brief comment which perhaps may be of interest to the committee. In drawing up this new bill we did a major operation on ministerial discretion. We practically cleaned them out of the Income Tax Act. One or two minor ones are left. We find that on doing away with ministerial discretion the only alternative is very complicated law. Now, perhaps it is not for me to say this, but it is a fact that there has been a great deal of comment on the extent to which the law is getting complicated. I am suggesting that the law has become more complicated as a result of doing away with ministerial discretion and spelling out in law exactness with respect to every situation. The old system, which worked very smoothly, was elastic, and there was no necessity for spelling out in such detail all the complexities in the law. I want to say that by way of explanation as to why the law appears to be getting more complicated than it used to be, but I think Mr. Gavsie is the man to explain the new system of depreciation.

Mr. CHARLES GAVSIE, Executive Assistant, Department of National Revenue: In doing so, Mr. Chairman, I would like to refer to a talk that I gave before a meeting of Chartered Accountants, and if you would permit me to read a relatively short part the explanation might come out. What I said was:

"One of the main objects of the new procedure is to ensure that a taxpayer will be allowed to recover the capital cost to him of property. This is a departure from the old procedure, particularly in that loss in value of assets from causes other than strictly wear and tear, such as obsolescence, will be recognized as a legitimate charge against income. That did not prevail under the old system. As a corollary to this, however, deductions from profits will not be allowed in excess of that portion of the capital cost which is ultimately established to have been actually lost. This means that if upon disposition of an asset it is found that the amounts previously allowed as deductions from income exceed the loss actually suffered, the excess will be brought back into income.

In the interests of simplicity it is proposed to establish a relatively small number of general rates of depreciation and it will be provided that these rates will be applied each year on what is known as the reducing balance method. Use of this method will entail substantial increases in the present straight-line rates of depreciation.

While, as stated above, the new procedure will allow a taxpayer to recover out of income what was formerly treated as a capital loss, it is proposed not to bring into income any profits arising as a result of depreciation having been allowed prior to 1949. To accomplish this end it will be provided that the capital cost of all property owned by a taxpayer at the beginning of 1949 will be the depreciated value according to the records of the department at the end of 1948 and that any proceeds on disposition of such assets in excess of that value will be treated as a capital profit. There will, however, be exceptions in the case of the sale of those assets subject to double depreciation or special depreciation granted by the War Contracts Depreciation Board.

In addition, in order to eliminate any possibility that the new procedure results in the taxing of capital profits, the excess of the proceeds from the disposition of any asset acquired in 1949 or thereafter over the original cost thereof will be treated as a capital profit.

As to the mechanics of calculations, a relatively small number of groups of assets will be set up, each group carrying a different rate of depreciation. The mechanics of the system will be that in each group the starting point will be the departmental depreciated cost at the beginning of 1949, to which will be added the cost of additions and from which will be deducted the proceeds of disposals during the year. The deduction to be allowed from profits in that year will be determined by applying to the figure so arrived at the rate applicable to that group, and the amounts so allowed will be deducted from the capital costs of that group to arrive at the starting figure for the next year. If, at any time, there is a credit balance in the account representing any group of assets, it will be transferred to income and subjected to tax.

If, at any time, a taxpayer has disposed of all the assets in one group and there still remains an undepreciated capital cost for that group, it will be allowed as a deduction from income in the year of disposal.

So that the thing works both ways.

Hon. Mr. EULER: Mr. Chairman, I would like to ask a question just there. It has been stated that the intention is not to tax capital gains, I think.

Mr. GAVSIE: Yes.

Hon. Mr. EULER: And I think that is the policy of the government. Now I would like to put to Mr. Gavsie a case which I think clearly proves that under this system capital gains will be taxed. Say that you, Mr. Chairman, buy a piece of real estate in a retail district in any one of our growing cities, for $100,000. You depreciate that for, say, a period of five years, at whatever the rate might be, say 3 per cent. In those five years you would have depreciation of $15,000. Am I right in that?

Mr. GAVSIE: We will take those figures as good enough for the example.

Hon. Mr. EULER: Then, let us say the property is sold for $150,000. You say there is a profit of $50,000.

Mr. GAVSIE: Oh, no. That is a capital profit.

Hon. Mr. EULER: I am just trying to get information. Will the $15,000 that was written off be subject to tax? Will that be included in the income of the year of sale upon which the tax has got to be paid in one sum?

Hon. Mr. MORAUD: Yes.

The CHAIRMAN: Perhaps we had better let Mr. Gavsie answer the question.

Mr. GAVSIE: If there is only one piece of property, the answer is yes.

Hon. Mr. EULER: This is one piece of property. My argument is that in the case of property of that kind depreciation is only on the value of the buildings, and not on the land.

Mr. GAVSIE: Yes.

Hon. Mr. EULER: There is no depreciation on the land. The amount of $150,000 has been obtained for a property which cost $100,000 in the first place. The $50,000 profit is made on the increased value of the land.

Hon. Mr. CAMPBELL: Certainly.

The CHAIRMAN: Maybe.

Mr. GAVSIE: Are you talking about $50,000 or the $15,000?

Hon. Mr. EULER: I am talking about $50,000.

Mr. GAVSIE: As I said before, $50,000 is capital profit, and we have no concern with that. We are only concerned with the $15,000 that the taxpayer took by way of depreciation; and he has now got a price in excess of the original cost, after having taken $15,000 depreciation.

Hon. Mr. EULER: Yes, but he got a price in excess of the original cost by reason of the value of the land, and not by reason of the value of the building on which depreciation was taken. Therefore, if the property increased in value to the extent of $50,000 it was because of the increased land value, and there has really been no profit on account of the building and yet the owner took a depreciation of $15,000 on it. As a matter of fact, the $15,000 is not a profit at all.

Mr. GAVSIE: Land is not subject to depreciation.

Hon. Mr. EULER: I know it is not.

Mr. GAVSIE: May I say that when I use the word "depreciation" I am using an incorrect term. The law provides for an allowance in respect of capital cost of property. This is an arrangement to obtain the return of capital outlay.

Hon. Mr. CAMPBELL: Out of income.

Mr. GAVSIE: Yes, out of income; that is the whole question. It is not depreciation in the old sense, namely wear and tear; it has now become merged with recovery of capital because, as I have said, we are now providing for obsolescence or any other loss.

Hon. Mr. EULER: But just take my question and tell us about the $15,000.

Mr. GAVSIE: If he had started off by breaking his $100,000 price down into so much for land and so much for building. Then on the sale of the property provision is made in section 7 that the amount of the sale price that is reasonably attributable to the building is to be determined. Of course if the taxpayer and the department do not agree on the value, he has a right to go to the Court.

Hon. Mr. MCLEAN: Lots of times the building is torn down on the property, because it doesn't represent any value.

Hon. Mr. EULER: The $15,000 depreciation on the building is a genuine depreciation, and if that is so it should not be subject to tax. Is there not a danger by reason of your taking that $50,000, which came about by the appreciation in the land values, when in fact the $15,000 represents a general depreciation in building only? You might say that because a man has sold his property at a big profit, he has charged too much for depreciation, and should be taxed further. I say again, that the depreciation, so far as the building is concerned, is a genuine one.

Hon. Mr. MACLENNAN: Can you separate the two items?

Hon. Mr. EULER: I do not know, I am asking the question?

Mr. GAVSIE: You would have to separate them.

Hon. Mr. HAYDEN: You can separate them; it is done often on expropriation valuations

Hon. Mr. EULER: I would like to know whether the department would separate them?

Dr. EATON: You would have to, both under the old and the new system.

Hon. Mr. EULER: If you taxed the $15,000, which is a genuine depreciation on buildings, you are certainly taxing capital gain, because the gain was made by reason of appreciation of the land.

The CHAIRMAN: Does that mean that in every case where there is a sale of real estate with buildings on it, that the problem would arise as to the distribution of the purchase price as between land and buildings?

Hon. Mr. NICOL: Mr. Chairman, may I follow up the last question asked of Mr. Gavsie? Suppose that he has a property worth $150,000, which is entered in the books in 1948 at that value; for a number of years the property has been devalued from year to year. By 1948 it stands in the books at a depreciated value say of $100,000, and in that year he sells the property.

Hon. Mr. MORAUD: 1949?

Hon. Mr. NICOL: No, he sells it in 1948.

Mr. GAVSIE: Would you put it 1949?

Hon. Mr. NICOL: Please wait for my question. He sells the property in 1948 for $150,000, and the new buyer is not aware of the loss when he pays that amount. When it comes to applying the loss would you take the value shown on the books in 1948?

Mr. GAVSIE: You mean for the new buyer?

Hon. Mr. NICOL: Yes.

Mr. GAVSIE: If the new buyer is a stranger—that is if he is not a relative—we will take the depreciation on what he paid, the amount of $150,000.

Hon. Mr. NICOL: The old depreciation is written off so far as the property is concerned?

Mr. GAVSIE: Yes, the new buyer starts at the price he paid.

Hon. Mr. NICOL: Then suppose he buys it in 1949, instead of 1948, and in the books of 1948 it was entered at a depreciated value of $100,000. He sells the property in 1949 for $150,000. Will the new buyer be assessed for the property on the $100,000 value?

Mr. GAVSIE: No, on $150,000. The new buyer takes his allowance on what he paid, namely $150,000.

Hon. Mr. DUTREMBLAY: Take for instance a property worth $100,000, which has been depreciated for five or ten years at say 2 per cent—

Hon. Mr. EULER: In five years it would be $10,000.

Hon. Mr. DUTREMBLAY: —and suppose its sale value under the municipal assessment is now $75,000. If the owner dies would his widow have to pay tax on the depreciated value, which is a loss of capital, and not a revenue? By reason of the government having frozen certain rates during the war years, the revenue has, as they say, gone with the wind. On this property with a sale value of $75,000 would the widow of the owner have the $10,000 depreciation capitalized against her?

Mr. GAVSIE: No.

Hon. Mr. DUTREMBLAY: If I remember the provisions of the bill correctly, there is a clause which states that when a person dies the proper value of the property will be taken.

Mr. GAVSIE: The individual would take this capital allowance under the new system. Should he die, there would be no recovery, and his heirs will take depreciation on the fair market value at the time.

Hon. Mr. HAYDEN: There are two problems there.

Mr. GAVSIE: With one recovery.

Hon. Mr. HAYDEN: One problem would be this. If the widow in the administration of the estate, for instance, sells a property and realizes what you might call a capital gain in relation to the original cost, then the recapture provisions would apply: is that right?

Mr. GAVSIE: Well, does she sell the property after she inherits it?

Hon. Mr. HAYDEN: She may be the administratrix or she may be the executrix of the estate, and in that capacity, before the proceeds are finally distributed, she may have to sell the property in order to get money to pay the debts and deal with the distribution. In those circumstances, if she gets a capital gain on the sale, that capital gain would be subject to the recapture provision?

Mr. GAVSIE: I don't understand what you mean by "capital gain".

Hon. Mr. HAYDEN: What I am talking about in saying "capital gain"—don't let us quibble on terms—is that she realizes on the sale price a larger sum than the original capital cost.

Mr. GAVSIE: We never tax that.

Hon. Mr. HAYDEN: Oh, yes, you do.

Mr. GAVSIE: No.

Hon. Mr. HAYDEN: Well, what you take is this: you take the lesser of the difference between the sale price and the then depreciated value, or the original cost and the then depreciated value—one or the other—you take the difference, and that is what you recapture in depreciation. That is very, very clear under section 7.

Hon. Mr. VIEN: Is that correct or not?

Mr. GAVSIE: That is not my understanding.

Hon. Mr. VIEN: What is your understanding?

Mr. GAVSIE: My understanding is, we are going to start with the 1949 costs—

Hon. Mr. HAYDEN: That is what I am talking about.

Mr. GAVSIE: Any amount in excess of that in the event of sale is a capital profit that is not affected in any way, shape or form—that is free.

Hon. Mr. HAYDEN: That is correct, but you recapture the depreciation. If when this widow receives the property and sells it—it may originally have cost $10,000 and that may be the value as of the 1st of January, 1949, but if the depreciation has been charged against that building to the extent of, say, $2,000, after 1949, then, if she sells it for the amount of the original capital cost of the 1st of January, 1949, or any additional amount, whatever it may be, to the extent of the difference between the original cost of $10,000 and the depreciated value of $8,000, that $2,000 would be recaptured depreciation and you would pay income tax?

Mr. GAVSIE: You have got me on a point I had not foreseen. But let me make this statement. Let us start with that property on the assumption that the 1949 cost is $10,000. The man depreciates it for two or three years, and it is down to $6,000. Then that man dies; the property passes to his heir, and then the heir sells it immediately after he gets title to it. There will be no recapture. If the heir kept the property he would be entitled to depreciate it at its fair market value, which might be substantially higher than its written-down value in the hands of his father.

Hon. Mr. HAYDEN: Where does it state that in the statute in relation to this special situation?

Mr. GAVSIE: Senator, we are in a most unfortunate position. What I told you is what I understand the regulations will be under section 11 (1) (*a*). We are in the unfortunate position that all there is in this bill is under section 7, a provision for recapture.

Hon. Mr. HAYDEN: No, no, there is more than that.

Mr. GAVSIE: Clause 8: there is a provision for calculation of capital cost.

Hon. Mr. HAYDEN: I am looking at section 7, (1) on page 5, which adds a new section 20, subsection 1. It says:

> (1) Where depreciable property of a taxpayer of a prescribed class has, in a taxation year, been disposed of and the proceeds of disposition—

That is, the sale price.

> —exceed the undepreciated capital cost to him as of the beginning of the year of depreciable property of that class—

Mr. GAVSIE: Yes. That is all the property of that class.

Hon. Mr. HAYDEN: But I am talking about this house in the hands of a widow. Then it says:

> The lesser of (*a*) the amount of the excess—

That means the difference between the sale price and the depreciated value of the property at the moment of sale, or the difference between the original capital cost and the depreciated value at the time of sale. Now, one or the other of these amounts, whichever is lesser, will be added to the income of the taxpayer for the year and will be taxed. That is what 7 (1) says.

Hon. Mr. CAMPBELL: Is that not the intention of the framers of the act, that starting as of January 1, 1949, any person who gets a tax benefit in respect of depreciation shall account, we will say, for any gain or any recovery that he makes in respect to that depreciation?

Mr. GAVSIE: Any recovery.

Hon. Mr. CAMPBELL: So that in that case, in the case Senator Hayden refers to, his original capital cost might be one hundred thousand dollars, his depreciated value as of January 1, 1949, being $50,000: in the next five years he takes a further $25,000 and then sells it for $75,000; he is accountable under the recovery basis for the $25,000, and he has got a capital profit which he does not have to account for of $25,000?

Mr. GAVSIE: That is right.

Hon. Mr. HAYDEN: That is exactly the question I was asking Mr. Gavsie. I said even in the case of a widow, unless there is a provision here—

Mr. GAVSIE: I think the answer to your question is that a disposition flowing from a death is not deemed to be a disposal.

Hon. Mr. HAYDEN: Where is that?

Mr. GAVSIE: Well, senator, all I can give you is my assurance that that flows from our discussion with the Department of Justice. The definitions deal with "disposition" and "proceeds of disposition". We discussed it with the Department of Justice, and we were told that the transfer of property flowing from death—

Hon. Mr. HAYDEN: I am not talking about the transfer flowing from death. I am talking about the value of the property in the hands of the widow. I am talking about the widow, who as part of the administration of the estate, sells the property, and she sells it for the original value as of January, 1949, or more than that; but for whichever of these two prices she sells, to the extent of the depreciation taken since the 1st of January, 1949, that will be recaptured and she will have to pay income tax on that.

Mr. GAVSIE: That she has taken. Not that her late husband—

Hon. Mr. HAYDEN: That she has taken.

Mr. GAVSIE: No, I am not prepared to agree with that.

Hon. Mr. VIEN: How do you reconcile that with section 20, subsection (1)?

Hon. Mr. HAYDEN: If your position in the matter is correct, then show me in the bill, because I will be very happy to know it is in there.

The CHAIRMAN: Will you put the question the other way, that in the case where the husband has taken depreciation after January 1, 1949, that is one case; the other case is where the widow has taken the depreciation after the date of the death of her husband. I think that is the distinction Mr. Gavsie is trying to make.

Hon. Mr. HAYDEN: I am not arguing the point. I would like to find that actual reference.

Hon. Mr. VIEN: The case that has been put by the senator is not with respect to the widow, it is with respect to the executor. If the executor, the widow or somebody else, is obliged to sell a piece of property on which, since the 1st of January, 1949, depreciation has been allowed, and this property has been sold by the executor at an increased price, that is at a price higher than the price established on the 1st of January, 1949, then section 20 (1) says: this difference, whichever is the lesser of the two, shall be included in computing the income tax for the year. The question is, shall the taxable income of the deceased person be increased by the amount involved?

Mr. GAVSIE: My answer is no.

Hon. Mr. VIEN: How, then, do you reconcile that with paragraph one of section 20?

Mr. GAVSIE: I think you will find that is covered by "disposition of property" which is found on page 6.

Hon. Mr. EULER: Why not say "sale"?

Hon. Mr. HAYDEN: You will notice that "disposition of property" includes any transaction or event entitling a taxpayer to proceeds of disposition of property.

Mr. GAVSIE: That is not a disposition of the property.

Hon. Mr. VIEN: It is a sale by the executor.

Mr. GAVSIE: What I am trying to resolve at the moment is, what is the position of the executor while he is the appointed representative of the deceased? I am trying to figure out for the moment whether he is taking any depreciation, because we do not deal with the different parties. We do not go back to 1949 if a different party is taking the depreciation.

Hon. Mr. HAYDEN: In the case of the widow who is the executrix, she has just succeeded to the property of the deceased person and she is holding the property. Then she sells the property.

Hon. Mr. MORAUD: That is an event.

Mr. GAVSIE: The event by which she gets the property is not an event which entitles her to the proceeds and the profits. May I say this. As far as I am aware, and in all the discussions that have taken place, there has been perfect agreement that there is no tax in that case. You have brought up a case where it is a little hard for me to say, "Here it is in black and white". I do not think the law provides for bringing back into income, under section 20, subsection 1, the proceeds of sale.

Hon. Mr. HAYDEN: By the widow?

Mr. GAVSIE: By the widow. That is my opinion.

Hon. Mr. HAYDEN: I think it does.

Hon. Mr. MORAUD: Yes. I think the court would decide differently.

Hon. Mr. HAYDEN: Are you prepared to make a statement that it does not?

Mr. GAVSIE: I am in the most unfortunate position because the regulations have not been passed by the Governor in Council. All I can tell you is that the matter has been discussed, and that the agreement amongst all the people charged with working this out is as I have outlined. Would you leave that question until we get the regulations out? I can only give you my explanation.

Hon. Mr. VIEN: No, we cannot leave it. We do not want to embarrass the officers of the department in any way, but there is one thing we want to know. We want to understand the meaning of the Act, which we are called upon to enact. Your regulations in the sphere you have just outlined, cannot go beyond the terms of the statute. We are finding that the statute, in our humble opinion and as far as we can construe it, would have an effect like the one that has been pointed out to you. If that is not correct, then the bill should be clarified so as to make it abundantly clear, because you cannot go beyond the statute in respect to legislation. It would seem to us that inasmuch as when a man dies, you question his returns for income tax. You very often re-open and re-assess his income tax for one, two, three or four years. Here is a case of a man who dies. The executor is obliged to sell a piece of property. He has the piece of property valued at $10,000. He has received $2,000 for depreciation. The executor sells this at $12,000, and then in terms of section 20, it would seem to us at first sight—and we want to understand it because we are from Missouri and want to be shown—that the department could tell the executor, "Look here, the deceased had this piece of property. It was valued at $10,000. We allowed $2,000 as depreciation. That depreciation of $2,000 has been taken out of his taxable income. Now, you have sold that piece of property for $12,000, indicating that indeed you have suffered no depreciation—that the deceased suffered no depreciation. We want to recapture that depreciation". That is exactly the question that was put. We want to be shown whether or not your section 20 would enable you, by regulation or otherwise, to say no in the case of a deceased. I should like an answer to this question.

Hon. Mr. MORAUD: I just want to say a word on this point. We are in the unhappy situation where we do not have before us the bill as passed by the House of Commons. On top of that, Mr. Gavsie speaks constantly of regulations that will practically amend the bill. In your regulation you give an interpretation of the definition of the word "event", and there is no doubt that it will be an amendment to the bill. I contend that in my province the death of a person is certainly an event that transfers property just as much as any other transaction. So that event, the death of a person, is certainly a transfer of property in my province.

Mr. GAVSIE: I am afraid you have misunderstood me. I said that the disposition of property includes an event entitling the taxpayer to the proceeds of disposition of property. I do not think you can just say it is an event by which property is transferred. I do not think that the passing by disposition of a will or by the rules of law is an event which entitles the taxpayer to the proceeds of disposition of property.

Hon. Mr. VIEN: What would be the nature of an event? Is not a deed of sale an event entitling the taxpayer to the proceeds of the disposition of a property?

Mr. GAVSIE: Yes. "Proceeds of disposition" of property include the sale price of property that has been sold, compensation for property damage, destroyed, taken or injuriously affected—

Hon. Mr. VIEN: Where do you find that?

Mr. GAVSIE: In the very next definition, on page 6 of the bill.

The CHAIRMAN: Would that not apply to a sale by an executrix or trustee of an estate?

Mr. GAVSIE: If the executor had not taken any depreciation, there would be nothing to recapture.

The CHAIRMAN: But you might have a case where an executor or trustee has taken depreciation since the estate has come into his hands.

Mr. GAVSIE: That part of the depreciation, that is depreciation taken by an executor or trustee since he came into possession of the property, would be subject to recapture, but what I thought the senators were talking about was depreciation taken by an individual during his lifetime.

Hon. Mr. HAYDEN: That is right. I was discussing the depreciation that had accumulated with relation to the property prior to the time that it came into the hands of the executors, and I was asking whether in the event of a sale by the executrix there would be a recapture of depreciation that the testator had accumulated in his lifetime.

Hon. Mr. CAMPBELL: Would you look at clauses (*a*) and (*b*) of subsection 1 of section 20, on page 5 of the bill? There it is provided that the tax will be on the lesser of the amount of the excess, or the amount that the excess would be if the property had been disposed of for the capital cost thereof to the taxpayer.

Hon. Mr. CAMPBELL: Until you recover your capital cost you are free of tax?

Mr. GAVSIE: If the amount of the excess is less than the 1949 cost, you take in only the excess. But if the amount realized on the sale is more than the 1949 cost you take in only the amount up to the 1949 cost, and the amount above that is free.

Hon. Mr. HAYDEN: But that does not deal with the question we were discussing.

Hon. Mr. VIEN: What we would like to know is what is meant by an event. If a man dies, that is an event?

Mr. GAVSIE: Yes.

Hon. Mr. VIEN: If he leaves a will, that is an event. If there is a deed of sale, that is an event. If a man dies you have no scruple against going back to his estate and revising his income tax returns for one or more years. So in the event of a man dying and his executor acting as we have suggested, could you not under these provisions take the stand that the deceased benefited from depreciation to which he was not entitled because his property has not depreciated?

Mr. GAVSIE: While it is true that we go back in the case of a deceased taxpayer, we go back to the period when he was alive. But in the absence of specific provisions to the contrary in the law, anything received after the moment of his death is not part of his income. The event that gives rise to the proceeds of disposition of property is a sale made by his executor after his death. My interpretation—and I offer it only as my interpretation—is that the event which becomes a disposition for the purposes of clause 7 is a sale made by the executor after the death of the taxpayer, and in my opinion—it is only my opinion—that sale would entail bringing back into the income of the estate only the depreciation that was taken by the executor or trustee after the death of the individual.

Hon. Mr. HAYDEN: You would have no objection, then, to making that clearer in this particular section?

Mr. GAVSIE: I do not draft these bills, sir. I do not wish to suggest that I am entitled to the credit for this language.

Hon. Mr. HAYDEN: Whose language is it?

Mr. GAVSIE: The language of the Department of Justice.

Hon. Mr. MACLENNAN: You say the Department of Justice?

Mr. GAVSIE: Yes.

Hon. Mr. MACLENNAN: That explains it.

Hon. Mr. DUTREMBLAY: If a man in his will devises his property to his wife, is that a disposition of property?

Mr. GAVSIE: No, senator. If you look at the bottom of page 6 and the top of page 7 you will find certain rules. Rule (*d*), on page 7, says:

> Where a taxpayer has given property away otherwise than by will, he shall be deemed to have disposed of it at the time of the gift at its fair market value at that time.

So if he gives it by will he is not deemed to have "disposed" of it. I would say that when property is devised by will there is no "disposition", and this rule goes further and says that there is no disposition even if it is given away by will. So there would be no recovery in the case of property passing by a will.

Hon. Mr. NICOL: Mr. Chairman, the explanations that were given at the beginning of this meeting divided the bill into three parts, and we were told the intention was to make a general revision of the Income Tax Act. Now, as I understand it, in the present Income Tax Act there is nothing similar to sections 7 and 8 of the present bill. No explanations were given as to why these sections should be in the bill, and I believe there was no understanding of them in the Senate or the other house.

The CHAIRMAN: Senator Nicol, to be fair to Mr. Gavsie, it should be pointed out that he did give us an explanation. Whether we accept it or not is another matter, but he has given us a general explanation.

Hon. Mr. NICOL: I think these two sections could be eliminated without changing the general economy of the Income Tax Act, and I move that the two sections be deleted.

The CHAIRMAN: We are not yet dealing with the bill clause by clause, and I think, senator, that it would be more appropriate to wait until we reach that stage before you move your motion.

Hon. Mr. NICOL: Mr. Chairman, questions are being asked and answered, and so far as I can see we are not making any progress. We will spend the whole morning on this bill, but the important parts are sections 7 and 8, which are amendments to the income tax law. I am prepared to make a decision with respect to those sections, and I move that they be deleted from the bill.

Hon. Mr. LAMBERT: May I ask the witness, Dr. Eaton, if this bill as a whole were held over until next session, and in the meantime, or before final decision was made, fuller consideration were given to it, would any embarrassment be suffered by the department? Personally, after listening to the discussion in the house yesterday and the remarks here this morning, one becomes sensitive to the fact that we at least have been rushed in this matter, and I think the other house also did not have an opportunity to give full consideration to it. It seems to me that this portion of the bill, at least involves administrative matters, and does not affect revenue. Would it be possible to apply next year, for the same measure, and if you wish date it back to the beginning of 1949?

Hon. Mr. EULER: Would those reductions take effect if the whole bill were thrown out?

The CHAIRMAN: No; I do not think Senator Lambert is suggesting that the whole bill be thrown out. He may have used that expression.

Hon. Mr. LAMBERT: I meant that at least sections 7 and 8 should be deferred.

The CHAIRMAN: You mean that part of the bill dealing with depreciation.

Hon. Mr. LAMBERT: These are the main sections of the bill.

Hon. Mr. CAMPBELL: It seems to me that when we consider the language employed in the drafting of the bill we run up against the question of exactly how the measure is going to work. Before we reject this new basis of allowances contained in sections 7 and 8, we must decide whether or not the principle involved is proper and beneficial to the community as a whole. It is desirable in that I think it provides a more workable and flexible piece of tax legislation which will have the effect of eliminating the objectionable ministerial discretions which the public protest so often.

I have a great deal of sympathy with anyone who tries to interpret this legislation. I know the officers of the department who are here will agree that a piece of legislation of this kind, which tries to spell out a law which has formerly been handled by ministerial discretions, must be complicated, and the regulations under it must be involved. I venture to say that irrespective of how long this matter stands, that unless the committee is willing to take the advice of the law officers and perhaps chartered accountants who are engaged in this type of practice, that it is a feasible and workable piece of legislation, it will never be passed. I do not think anyone who is inexperienced in tax matters can possibly read these sections and understand the meaning of them. Further, I do not think it is possible to draft any law to be so clear and concise as to show the proposition of law on which allowances are to be made in cases of this kind.

It seems to me that if we are going to accept the principle and consider this new piece of legislation, we should pass it with the assurance from the Minister and the Department that when it is put into effect should they find any great hardship or situations arising to which the law does not properly apply, there will be an opportunity for us to consider the question further next year.

Hon. Mr. NICOL: We will have the regulations.

Hon. Mr. CAMPBELL: With great respect, I am sure the regulations will not help the members in the interpretation of the sections, and to understand fully the meaning of their application.

I am sure there will be many problems arise under this new legislation, after it is passed. There always have been problems under our tax law. We in this house made an extensive study of tax laws two years ago, and I think the report brought down at that time was beneficial and helpful in enabling the department to bring forward last year an income tax act which was certainly a considerable improvement over the old act. The proposed legislation represents a step which could not be embodied in the act at that time.

I am convinced that so far as industry and business generally in the country are concerned, that the principle of this proposed legislation is good. I do not say that it will work as well in the case of individual property holders who buy property for investment purposes, carry it for five or ten years and then dispose of it. I would suggest that before the committee decides to reject these particular clauses of the bill, that we should hear from the Minister of Finance, and that we should give serious consideration to the proposal I make now, namely, that we accept the principle of the bill and adopt the legislation with any changes that we think are necessary; and further that we ask that the matter be thoroughly considered and if it is the wish of the house, a special committee could be set up to study the workability of this measure when Parliament meets at the next session.

Hon. Mr. EULER: Did I understand Senator Campbell to advise the committee to pass this legislation, but that he did not understand it.

Hon. Mr. CAMPBELL: No.

Hon. Mr. EULER: That is what you said. You said that you did not understand the bill but that you advocated its passage.

Hon. Mr. CAMPBELL: I say we must understand the principle of the legislation.

Hon. Mr. EULER: Well, we do not.

Hon. Mr. CAMPBELL: I think if we are patient enough Mr. Gavsie and Dr. Eaton can assist us.

Hon. Mr. MORAUD: The trouble is our patience cannot last more than one day—then the session is over.

Hon. Mr. DAVIES: It is quite evident that this proposed legislation is very complicated. Then is it fair to the ordinary citizen of Canada to put into effect a portion of the income tax which he does not understand? Is it fair to ask the ordinary, average Canadian citizen, should he have a little property or become involved in any of the provisions of sections 7 and 8, to go to some expert and pay him real money before he can make out his income tax returns?

We have around this table some of the most able corporation lawyers in Canada, and they do not appear to understand this legislation.

May I ask a question: Suppose I am in the process of making out my income tax return, and become involved in some of these complicated provisions, may I go to the Inspector of Income Tax at Kingston, for instance, and ask him to clarify the matter and help me make out my return, or would I have to go to a tax expert and pay him?

Mr. GAVSIE: You could certainly go to the Inspector at Kingston, and ask him any questions you wanted to know. I don't know whether it is proper for me to say anything while this discussion is going on—

Hon. Mr. LAMBERT: Say what you like.

Mr. GAVSIE: There are five pages of writing in this bill, or perhaps more, and in excess of three-quarters of it relates to specific rules that do not affect the ordinary taxpayer. Take, for instance, an ordinary taxpayer who runs, let us say, a newspaper.

Hon. Mr. NICOL: No ordinary taxpayer runs a newspaper.

Hon. Mr. LAMBERT: A boot and shoe store.

Mr. GAVSIE: Yes, a boot and shoe store. He has fixtures in the store, may own the building and perhaps has an automobile. All he has to do is take one sheet of paper and divide it into three parts. He takes the building which, we will say, he has owned since 1935, and on which depreciation has been taken up to date; he has a record of that. Say he paid $10,000 for the building when he bought it, and he has taken depreciation up to 1949 at 2½ per cent—that would be 30 per cent. Then the 1949 cost of the building would be $7,000. He started this business in 1935. His fixtures cost him $15,000. He has been depreciating them at 10 per cent. He has taken all depreciation, so we are not concerned with any recapture or anything else. I am making this, of course, over-simple. He may have bought things in the meantime. Let me deal with a simple case. In 1945 he bought an automobile, or a truck—because if he had bought it in 1935 there would not be much left to it. It cost him $1,500.

Hon. Mr. NICOL: Where did he buy it?

Mr. GAVSIE: Well, say General Motors. Let us say that the 1949 cost of that is written down to $700. Well, now, what does he do in 1949? There is to be issued a regulation giving the rates. I cannot forecast what that will be. But he looks at the rate table and he says, "My building has a 1949 value of $7,000. I take 5 per cent of that, that is $350 for the building. The fixtures have been fully written off; there is no depreciation for this year on the fixtures. My automobile, $700, the rate for that is, say—20 per cent; I take $140 for depreciation on that. My depreciation for this year is $490." So in making up his income tax return he has got $490. Now he comes to 1950. He has taken $350 as his depreciation for 1949. $7,000 was his 1949 cost. That gives him $6,650. Now, for 1950 he takes 15 per cent, if that is the rate, of $6,650, and that will

give him in the neighbourhood of $300—I am not very good at arithmetic. There is no depreciation on the fixtures. He goes to the automobile; he took $140 depreciation in 1949, so that the automobile is now written down to $560. The rate is 20 per cent. He takes 20 per cent off $560. He has got $300-odd depreciation on the building, and $70, or whatever the 20 per cent of $560 is, he adds that to it; that is his rate for 1950. Now he goes on till he sells something or buys something. If he buys something he just adds the price he paid for that article to that $6,650, if that is the balance at the end of that year. If he sells something, all he has to do is look and see whether the 1949 cost and the price he is now getting for it—if he is now getting more than the 1949 cost. Then he would take that off—, that is pure capital gain. If the price he got was less than the 1949 cost he subtracts that from $6,650. And here is the most important part of the new system, which never existed before. If he sold that article at a loss, heretofore he would have not have had any way of recovering that loss. Under this system the capital cost of that item is included in the $6,650, and if he sells it or scraps it and only realizes a dollar for it he just deducts a dollar from the $6,650, and he continues to take depreciation on that amount, and continues to take the allowance. That was never provided for before. Supposing some of the things he is depreciating become obsolete and he has to scrap them. Under the old system, whatever he did not depreciate he would have lost.

Hon. Mr. Moraud: But there is the other side of that.

Mr. Gavsie: Oh, yes, there is a two-way street. If he recovers he has got to bring it back in. I do not know if I have answered Senator Davies' question. Naturally I have taken the simplest illustration. There might be two or three buildings in one group.

Hon. Mr. Nicol: If he loses he continues to take depreciation from year to year?

Mr. Gavsie: Yes.

Hon. Mr. Nicol: But if he makes a profit he pays it all at once, the same year?

Mr. Gavsie: No. He brings it first into that group. If he cleans out the group, if he sells out—

Hon. Mr. Nicol: But you spoke of one property. Let us keep to one property. He sells that one property and he loses. He continues to write off his loss from year to year?

Mr. Gavsie: No, if he has only got one property, if he loses, that is a loss against his income of that year.

Hon. Mr. Nicol: But if he makes a profit?

Mr. Gavsie: Up to the extent of the allowance he has taken he brings it back into income.

Hon. Mr. Moraud: I want to stop with that case, and I wish you would think of some amendment to protect those people. I am thinking of the small property owner. If a small man buys a mining stock he is entitled to a depreciation, to a depletion.

Mr. Gavsie: You mean a share of stock?

Hon. Mr. Moraud: Yes.

Mr. Gavsie: There is no capital allowance for that. There is depletion, senator.

Hon. Mr. Moraud: If he buys a bond he gets his interest; no depreciation, no nothing. In my part of the country a lot of these people are small property owners. They buy a small property instead of buying a bond. It is their investment. They have a large family. The property owner takes his depreciation

of two and a half or five per cent or whatever it may be and uses it. Now after five or ten years he sells the property. Well, you come along and you tell him, "Now, you have taken 5 per cent during those ten years, you have sold that property at a profit, you have made an investment, you have not had any interest on it, except that you have taken depreciation. Now you are going to be taxed for that ten years' depreciation, and all at once, all in one year." Could you not do something about it?

Mr. GAVSIE: Well, senator, perhaps this may not be the answer, but it is another thought that you should take into consideration, that under these rules the person is not obliged—supposing in any one year the property brings in some income, the next year maybe it is vacant for part of the year—the person is not obliged to take any particular part of the depreciation.

Hon. Mr. MORAUD: No, but he has to in my case. He is a poor fellow, he has to take it, it is part of his income. Instead of taking 3 per cent on a bond he takes the two and a half per cent which is allowed as an expense apart from the depreciation. The depreciation or what we call depreciation here is the recovery of the capital cost. Let us assume that the rent is $1,000, that his interest on his mortgage and his taxes and his repairs come to $1,000. He would be ill advised, unless there was some other reason, to take any depreciation.

Hon. Mr. MORAUD: You do not figure the interest on the money that he has invested, the interest that he would get if he bought a bond.

Mr. GAVSIE: I am afraid that is a question of policy I do not want to get into.

Hon. Mr. EULER: I should like to ask a question in view of Senator Nicol's motion. It may influence us to some extent. It was stated, either by Dr. Eaton or by Mr. Gavsie, that the two controversial clauses, 7 and 8, dealing with depreciation, are the direct result of the taking away from the minister the powers of discretion—practically all of them.

Hon. Mr. VIEN: The powers to make regulations.

The CHAIRMAN: It is not the direct result.

Hon. Mr. EULER: I think Dr. Eaton did say that the reason why some of this legislation is necessary, is a direct result of these powers of discretion in a large measure being taken away from the minister. Am I right?

Dr. EATON: Well, yes.

Hon. Mr. EULER: Now, we certainly do not want to reject the whole bill because I suppose that would wipe out the reductions in taxation. Therefore, the only question in issue is based on these two sections, 7 and 8. If we did eliminate these two sections would the bill then become unworkable for the reason he has stated?

Dr. EATON: I should like to clarify the first point. The change over in the system from what has been described as the old straight-line method of the diminishing balance principle, is not what has made the law necessary. There would have been a complicated law, even if we had not changed the system of depreciation. That is the point. We took away the discretion under which depreciation allowances were granted in the past, and as the result of that there had to be a new law of depreciation of one kind or another.

Hon. Mr. EULER: If these sections did not carry would we have a way of dealing with this matter?

Dr. EATON: We would still have to have regulations. The two things coincide, the fact that the ministerial discretion was taken away meant that there had to be specific authority for depreciation.

Hon. Mr. EULER: If these two clauses were left out what would happen?

Dr. EATON: There would have to be regulations made under section 11 (1) (*a*). I cannot say whether there would have to be anything in addition to that to make the old system work.

Hon. Mr. VIEN: No. It is working at the present time.

Dr. EATON: It worked up to the end of 1948.

Hon. Mr. VIEN: What are the difficulties in the working of the present system of depreciation? Sections 7 and 8 are intended to make a change, but is the Act not workable now?

Mr. GAVSIE: I would not like to answer that question right off the bat.

Hon. Mr. VIEN: I believe that the Act would be workable because it is workable at the present time. Am I not right that if sections 7 and 8 are changed there are correlated sections that will also have to be changed?

Mr. GAVSIE: There is a repeal at the beginning of clause 7. That would have to be maintained so as to repeal the old section 20. It relates to an entirely different subject.

Hon. Mr. VIEN: Well, the difficulty is to understand the incidence of the new system of taxation and depreciation. It cannot be clearly explained to the committee unless we have some specific cases and unless the officers of the department, who are here to enlighten the committee, are allowed to give full and clear answers to these specific cases. Take, for instance, the specific case proposed by Senator Moraud. A small property owner has a property worth $10,000. For two or three or four years the property is depreciated to the extent of $3,000 or $4,000. Then the owner sells that property for $12,000. Therefore, he has suffered no loss. He paid $10,000 and the increased value on properties generally has increased the value of his property. What do you do with a small taxpayer who has a small property? If we understood correctly the terms that were given this morning, you would have this taxpayer bring into his taxable income for the year, say, 1950, the amount of depreciation which he will have deducted from his taxable income from the 1st of January, 1949.

Hon. Mr. MORAUD: And he would lose the interest on the money that he has put up.

The CHAIRMAN: If he has otherwise recovered his capital.

Hon. Mr. VIEN: Senator Moraud has put a specific case. A very good way of understanding an Act is to find out what the Act does in respect to a specific case. Here is Mr. Jean Baptiste Trudeau who has a property of $10,000 on the 1st of January, 1949. On the 1st of January, 1951, he sells that property for $12,000. He had deducted the depreciation in 1949, in 1950, and in part of 1951. Then he sells the property for $12,000.

Mr. GAVSIE: Is this property rented?

Hon. Mr. VIEN: Whether it is rented or whether he has occupied the property himself, it is the same.

The CHAIRMAN: Oh, no.

Hon. Mr. VIEN: Take it as being rented property then.

The CHAIRMAN: There is no depreciation on property which the owner occupies himself.

Hon. Mr. MORAUD: It has got to be rented property.

Hon. Mr. VIEN: Well, suppose it is rented. That property has depreciated and it is deducted from his taxable income for the time being. He sells that property at a price higher than the value fixed on the 1st of January, 1949. Then he will be called to add to his taxable income for 1951, the year in which the sale is transacted, the whole of the depreciation that he has enjoyed from January 1, 1949.

Hon. Mr. MORAUD: And he would have lost the interest on the money he has invested in that property, so he would be better off to buy bonds.

Mr. GAVSIE: May I ask a question. During the years he took depreciation he had income from the property but had he not taken the depreciation he would have paid tax on it, so instead of paying a tax he takes this amount of depreciation. Is that the case?

Hon. Mr. MORAUD: No. Let me put it this way. We have a lot of these people in my city. Let us remember that many French Canadians do not know much about bonds or stocks. Perhaps you read in the newspaper recently that a man in Montreal had $100,000 hidden in a pail. There was a hold up but the fellows made a mistake and took the wrong pail, so the man kept his $100,000.

Hon. Mr. MORAUD: These people come to the city from farms, raise large families and buy themselves a house with a couple of tenements. They do not get any interest on the money that they invested in the property, but they are allowed to write off depreciation at 2½ or 5 per cent a year. Well, when a man sells a property after he has held it for some years, the department can come along and say: "You have written off two and a half or five per cent every year while you have owned this property and you have depreciated it by $5,000. Now you have to pay a tax on that $5,000, and you have to pay it all in one year." Well, that will discourage people from investing in real estate.

Hon. Mr. BURCHILL: Mr. Chairman, I think this has been a most interesting morning. After having listened to the discussion in the Senate yesterday I came here feeling very much opposed to sections 7 and 8 of the bill, but after listening to the clarification which has been given by the departmental officials I am inclined to think that the proposed new method is not as bad as we think it is, and that if we were more familiar with it we would perhaps like it. I have been thinking about the effect that it would have on not only small property owners such as Senator Moraud has in mind, but on small businessmen and primary producers, who in our section of the country are most important. It seems to me that if they became familiar with what the department is proposing they would like it. I say that for this reason. In our section of the country we do not make profits in business every year. In fact, there are many years when we operate at a loss. And as I understand the provisions of this section, it would be optional with the businessman to charge depreciation or not, as he wished. If a businessman had a tough year he would not be obliged to charge depreciation. Indeed, after listening to the explanations that have been given here, it seems to me that a man might be asking for trouble by charging depreciation, and that if he can get along without charging depreciation he will be better off. So this might appeal to the young man starting out in business, the fellow we want to encourage, because at the start he would not have to set aside any reserves for depreciation. I think it would also appeal to the primary producers and to all businessmen who are not sure of making a profit every year.

The difficulty is, as one of my colleagues here has said, that the proposed method is so abstruse that we cannot understand it. It has taken me, and I am sure many of us, several hours to see just what is intended. I think it would be highly beneficial if we could get the idea behind the system across to people in businesses, both small and big, and get their reaction to it, for I am quite sure that Canadian businessmen as a whole are not familiar with what is proposed in these regulations. While I am in favour of the new scheme and think it will work out for good, I would suggest that until business people are able to familiarize themselves with it and express their reactions, it would be most beneficial to postpone enforcement of the regulations for the time being.

The CHAIRMAN: In view of our difficulty in understanding the principles involved in sections 7 and 8 and in their application, I thought it desirable to ask the minister to come in. Perhaps it would be well to suggest that he devote any explanation that he may care to make to these two sections.

Hon. Mr. LAMBERT: May I suggest that the minister deal with the proposal that sections 7 and 8 be dropped from the bill at this time.

Hon. Mr. NICOL: Before the Minister speaks I wish to point out that I made a motion earlier that sections 7 and 8 be deleted from the bill. From the explanations that we have received this morning I understood that the deletion of these two sections would not change the general economy of the bill, which is a bill to amend the Income Tax Act. When this meeting began we had before us only a copy of the bill as read the first time in the House of Commons, but now a distribution has been made of the bill as read the third time. The explanatory note opposite clause 7, on page 5 of the bill, says that the new section 20 carries out the new scheme for depreciation which is being adopted by regulation, and the note opposite clause 8, on page 8, says that the provisions in this clause are transitional to establish the initial position of taxpayers for the application of the new principles of depreciation. I submit that these new sections 7 and 8 could be deleted without making any change in the general economy of the bill.

Hon. DOUGLAS C. ABBOTT, Minister of Finance: Mr. Chairman, first I apologize for my delay in getting here, but I had to attend another meeting. I will not attempt to discuss the point raised by Senator Nicol's motion that sections 7 and 8 be deleted, as it would perhaps be better if I addressed myself more to the substance of the new scheme and the suggestion that further time be allowed for consideration of it. First I want to point out that the fundamental principle is found in section 11 (1) which makes it possible to allow depreciation. Depreciation is a concession which is made to the taxpayer. The tax gatherer might say to the taxpayer, "You cannot take depreciation at all but must pay the tax on your gross income." Depreciation was allowed under the Income War Tax Act, but the rates of depreciation and the method by which it could be taken were left to the discretion of the minister. The committee realizes that the minister could say, in effect: "You cannot take any depreciation at all, or you can take it on the straight-line method, or on the diminishing balance method or on any other method you like." In our amended act which we brought in last year we eliminated as many as possible of these purely ministerial discretions and provided that such matters as depreciation would be determined by regulation.

Last March, when I presented the budget originally, I announced that it was proposed to introduce a new basis of allowing depreciation. I stress again that the allowance of depreciation was discretionary with the government of the day. It is not mandatory but is a concession to the taxpayer. It is reasonable to allow it and it has always been allowed, but I think the basis on which it is allowed must be a matter for determination by discretion or some other method. The new basis has been, I know, extensively studied by groups such as accountants' associations, bar associations, the Canadian Manufacturers' Association and others interested, and we have received many representations and had numerous discussions about it. I think it also fair to say that we have had no serious criticism of the proposed measure from the organized representatives of business. That is fair, is it not, Dr. Eaton?

Dr. EATON: That is quite fair.

Hon. Mr. ABBOTT: I was talking to Mr. George Currie, an old friend of mine, last night, and he said he was quite satisfied with the new proposal.

I come now to the two sections of the bill with which the committee is concerned. Section 7, which enacts section 20 and subsection 1 gives statutory recognition to what we loosely refer to as the recapture principle. The remaining subsections are largely definitions.

Section 8 is a transitional section, setting out certain rules with respect to the initial portion of the assets, and the process of arriving at values at which one will start to depreciate. As has no doubt been indicated by Dr. Eaton and Mr. Gavsie, the provision of the new system will not be retroactive. Whatever depreciation has been taken, on whatever basis, up to the present time, will prevail. There is to be a transitional measure in the regulations, I am informed, which permits the taxpayer to take the dollar amount of depreciation in the initial year of 1949 on either the old straight line basis which he has been using, or on the basis on which it would be calculated under the proposed new system.

I am personally convinced, after some considerable examination of this new basis, that it is more beneficial to the taxpayer—certainly more beneficial to the honest taxpayer. It prevents some abuses which have existed in connection with depreciation. I am sure the members of this committee realize that the greatest opportunity for playing about with one's income tax is in his depreciation account and inventory account. I think that this new basis provides a more sound and fair basis to establish depreciation.

Mr. Stuart, the member for Charlotte, put his finger on a point which illustrates that the new basis is beneficial to the small taxpayer. He asked the question, "What about the fisherman who instead of buying a Diesel engine for his boat, buys an old automobile engine and adapts it to operate his fishing boat; he runs his boat so hard that he wears out three such motors before he can write them off on the straight line basis of depreciation? Is he helped by the old system?" I replied that under the old system he would not be helped, but under the new system he would.

I am now answering Senator Lambert's question, if I may, as to whether if we were to allow further time for consideration by the business community, would we get different representations than we have already received, the overwhelming majority of which has been in favour of the new basis.

So far as the farm group is concerned, we have had no representation from any agricultural organization of the community. For the first time in the house the other night, various members, some of them farmers themselves, expressed the view that this arrangement would be less advantageous to the farmer than the old system. Personally, I do not share that view, that is, assuming the farmer keeps the proper books and records. As we know, the small farmer usually keeps his record in the back of an exercise book, and it is not very complete. He has become accustomed to the old line method of allowing depreciation. There is perhaps an advantage, where he has under-depreciated a piece of equipment, to get benefit under the new system; nevertheless, if he likes the old system, why should we force him to adopt the new? The revenue from the farming section of the community is not great in any case. For that reason, I introduced an amendment to that section, which is the recapture provision—the pooling system of assets—that it should not apply to farmers and fishermen. I included fishermen because, under the income tax act, special treatment is accorded to them by allowing them to average profits over five years.

That is a general statement as to the reasoning which led up to this proposed change, and the circumstance which caused the government to introduce it. As I say, the reason I announced it last spring was that I was pretty sure at that time that the income tax bill would not be through before the end of March, and there would be ample opportunity for those interested in it to study it. I may say that the question of depreciation is, in its application, very complex. Its principle is extremely simple—just like A, B, C. You are entitled to deduct from your gross income an amount to represent what is considered a return of capital out of annual income. That is all there is to it. It is done in a variety of accounting ways, but in practice the underlying principle is that you would not tax as income part of the

returned capital. When one comes to apply the principle it is a different matter. Then of course we get into, as we all know, very complex situations, and a trained economist is very much better able to explain it than a lawyer.

Hon. Mr. LAMBERT: The regulations that Mr. Gavsie spoke of have not been definitely formulated yet?

Hon. Mr. ABBOTT: They could not be, because they are provided under the statute, which is now under consideration. I am informed that they are in pretty good shape.

Hon. Mr. LAMBERT: They have been discussed.

Hon. Mr. ABBOTT: Yes; they are pretty well drafted. It should not take very long to complete them and bring them before the cabinet when the bill has been passed.

Hon. Mr. LAMBERT: I suppose it is fair to say that the regulations really represent a good deal of discussion.

Hon. Mr. ABBOTT: They represent this, Senator Lambert, that the same thing that the income tax department used to do by simple decrees or ministerial discretion is, under our new system, to be enacted, passed by cabinet council; they will be published in the official gazette, and become public knowledge to everyone. Representations can be made by a taxpayer, should he feel the regulations are oppressive, unfair or inaccurate, to have them amended, in the same way as he could ask to have a statute amended.

All of us who have had any experience in the practical application of tax law know that rigid statutory provisions cannot always be laid down; there must be a certain degree of flexibility in the operation of the law, otherwise there is real injustice to the taxpayer. I know that lawyers, experienced in tax matters, recognize that to be the case.

Some have had the view that we have perhaps gone a little too far in eliminating discretions, but I do not think we have. I do not care for it; I think it is important that every taxpayer should know the kind of treament that is being obtained by others.

Hon. Mr. LAMBERT: The theory has been expressed by some that these depreciation clauses, 7 and 8, represent the thin edge of the wedge towards capital taxation, or a tax on capital gain. For instance, a man sells a property at $10,000 which he has depreciated to $5,000. The tax that would come into play in that case would apply to a certain extent as a capital gain tax.

Hon. Mr. ABBOTT: No; it is completely inaccurate to say that this so-called recapture principle involves anything in the nature of capital gain tax. For instance, a man who has a house, a piece of machinery or any other asset, takes his depreciation on it, and later sells it for more than he pays for it. In that way he makes a capital gain, but he has taken depreciation based on the assumption that he is getting year by year a return of his capital; and if it turns out that he has gotten greater return than that to which he was entitled, obviously he cannot have his capital both ways. On the other hand, under the new system, if he has under-estimated the amount of his depreciation, then he gets the benefit of that loss, or what would appear to be a loss, and he is entitled on realization to take what is in fact the real depreciated value of the asset.

Hon. Mr. EULER: Do you not think it is rather an onerous thing for a man who sells a property, after six or eight or ten years of taking depreciation, that you then recapture that, and that he has to pay the tax on that aggregate sum all in one year at the rates of that particular year?

Hon. Mr. ABBOTT: In practice, of course, he would not have to do that. It would be added back into his asset account, and I think I am correct in saying that the ultimate liability in the case of a business man really comes at the time when he finally goes out of business. That is really what it amounts to.

Hon. Mr. HAYDEN: But take a lot of these cases where the asset is the one asset he has, so you have not a "class of asset".

Hon. Mr. ABBOTT: Unless he is going out of business it is usually replaced by a new one.

Hon. Mr. HAYDEN: I am thinking of a man who has rented a house. In that case there is one house.

Hon. Mr. ABBOTT: He is not in business. But if he has taken out of income on which he should have paid tax more depreciation than in fact has been incurred by his asset, I see no reason why he should not be taxed.

Hon. Mr. HAYDEN: But the problem is you are taking the full amount in one year. That might have two effects. One is that the rate of tax may be higher in that year than when he accumulated the depreciation. The other is that taking the whole amount in one year would put him in a different bracket income-tax-wise than he would be over a period of years.

Hon. Mr. ABBOTT: That is possible.

Hon. Mr. VIEN: Would there be any insuperable difficulty in providing that this would be thrown back to his taxable income over the same period of years as the period of years during which he has been drawing depreciation?

Hon. Mr. EULER: And at the rate of those years?

Hon. Mr. ABBOTT: That is the sort of thing that would be covered by the regulations, not by the statute. But off-hand, I don't suppose—it certainly would not be impossible.

Hon. Mr. VIEN: May I draw your attention to section 7, where it is said that it shall be included in computing his income for the year?

Hon. Mr. EULER: That could not be touched by regulation.

Hon. Mr. VIEN: That would have to be amended.

Hon. Mr. ABBOTT: Yes, that is right. The regulations, I am told, are not yet completed. They cannot be until the necessary statutory authority is provided. They will substitute for what was a pure ministerial discretion before. I think they are pretty nearly ready; I am told they are: I would hope that the department will have them out before the end of the year.

Hon. Mr. DUTREMBLAY: Regarding the amount of depreciation that we used to pay on property, that would be changed, I suppose.

Hon. Mr. ABBOTT: Well, because of the use of the diminishing balance principle rather than the straight line, I suppose there will be some adjustment of rates, and higher percentage rates will have to be adopted. The mathematics of the thing would indicate that. But I assume that the new rates will be such as to correspond with existing rates if these rates are considered adequate. It may be in some cases that as a result of experience existing rates applied on the straight-line basis should be increased, should be higher. I don't know that.

Hon. Mr. DUTREMBLAY: That would be very important for people who have property.

Hon. Mr. ABBOTT: I think it is safe to say that the rate of adjustment will not be on a basis prejudicial to the taxpayer.

Hon. Mr. HAYDEN: In the light of Senator Vien's question which followed the proposition I put to you, in that section 7 the addition of several words would permit you to deal with it by regulation. If, after saying it shall be included in computing his income for the year, you would add the words, "or otherwise as provided by the regulations," you would have the situation covered.

Hon. Mr. VIEN: The regulations would be by order in council.

Hon. Mr. ABBOTT: Yes, of course, and published, senator.

Hon. Mr. VIEN: But that might not be as flexible. There might be an amendment to provide, over a period of years, and at the same rate.

Hon. Mr. ABBOTT: I would like to give some consideration to that. I have been talking to Mr. Gavsie. It is true that this applies to the 1949 period, but in the 1949 period the taxpayer, as I said, has the option of using the dollar depreciation to which he would be entitled under the old discretionary regulations, so that, as in some other points that have arisen in connection with small businesses, I promised to give consideration to these points and if necessary introduce an amendment in my spring budget making it effective for the current fiscal period. I would prefer to deal in that way with this point, because it is an important one as it would involve reopening assessments for previous years, and perhaps complicated questions of interest. Ordinarily it would be fair to do this. I quite see that. But I would not like—

Hon. Mr. VIEN: We do not ask that the assessments be reopened, but that that amount of money which must now be added to the taxable income be spread over a period of years in the future.

Hon. Mr. ABBOTT: What might be a satisfactory solution would be perhaps that we could push it forward over a period of years rather than going back; that is, have some basis of averaging in forward years. We had somewhat similar problems in connection with the excess profits tax, and where the boards of referees had to change the basis we had some quite complicated questions of averaging those back into previous years.

Hon. Mr. VIEN: The amendment suggested would enable you to deal with this matter by regulation.

Hon. Mr. ABBOTT: Well, would the committee allow me to consider a possible amendment as to that? I would hope that we would not try to rush it in during this session. We are going to have budgets closer together than we ever had before. I am assuming that I will be able to bring the 1950 budget in during April at the latest, so that we will not be here all summer. You see, any amendments of this kind which come in as early in the spring as that can be made effective for the 1949 period, because no assessments would have been made; and while books may have been closed, it is not at a point where they could not be reopened. Since it is not retroactive, there could be almost no recapture provision for the first period anyway.

Hon. Mr. GOUIN: We have been discussing the case of a certain sale, and as you are familiar with our system in the province of Quebec I think it would be easy for you to appreciate the situation. Suppose a man died on January 1, 1949, and left a small property. Say it was worth $10,000 and the amount of depreciation was $4,000. Then say the executrix, the widow, sold that property for $12,000. The cost was $10,000, the depreciation amounted to $4,000, and so it stood at $6,000 on January 1, 1949. I would interpret the Act as meaning that the estate would have to pay on the lesser of the two amounts: either the difference between the sale price of $12,000 and the cost price of $10,000, or the difference between the sale price and the depreciated amount.

Hon. Mr. ABBOTT: In the case that you are citing I take it that this would be a rented property?

Hon. Mr. GOUIN: Yes.

Hon. Mr. ABBOTT: Which had been depreciated up to January 1st down to $6,000?

Hon. Mr. GOUIN: Yes.

Hon. Mr. ABBOTT: For the purposes of this Act the value of the property would be $6,000. If it were sold for $12,000 it would be a capital gain so far as $6,000 is concerned, because we do not go back of January 1, 1949. In the example you have given the executrix could sell the property in question for $100,000 and be subject to no tax.

Hon. Mr. HAYDEN: It would depend upon when it was sold. If she sold it in 1951 the reduction would be the amount of depreciation taken in the interim.

Hon. Mr. ABBOTT: Yes, from the 1st of January, 1949, to the 1st of January, 1950, which might be a few hundred dollars.

Hon. Mr. MORAUD: You have given an exemption to fishermen and farmers. Could you not give a small exemption to the small property owners? I discussed such a case before you came in. In our part of the country, up to the last war, our people did not believe much in stocks or bonds. They did not know anything about them. They came from the land to the city because there was no place for them on the farm. In the city they were small wage earners and bought themselves houses for their familes. At the same time these houses were such that they would give them a certain small yield. If they had bought bonds there would have been no depreciation, anad they could sell their bonds without paying any taxes on depreciation. They sell that house at a profit, but they have had no interest on their money during the time the house was used. They sell the house at a small profit that they need for their large familes. Could there not be a limit of exemption for these small property owners?

Hon. Mr. ABBOTT: I would be very glad between now and the time I introduce my next budget, to see whether one might provide an exemption for the property owner who is not using his property in his business—that is to say, a person who holds real estate for an investment—as to whether on that type of property the old straight-line basis of exemption could apply. I should not like to make that decision now, because I never like to make snap decisions in cases of this kind. Since we are in the position where any change which is made in March or April, 1950, can be made applicable to the 1949 period, I do not think anybody will be hurt. I do not want to commit myself, but I will be prepared to give serious consideration to that type of small investment holder. If I were doing it would I restrict it to the owner of only one or two rented properties? What I mean to say is, if it were sound in principle, as it might well be for the small real estate investor, it might be equally sound for the larger investor. This new basis is applicable particularly to the fellow who has got a fluctuating inventory of equipment and buildings, and so on, where under normal circumstances, if he gets rid of one, he buys another the next day in order to keep his business going.

Hon. Mr. HAYDEN: It goes further than that in a way.

Hon. Mr. ABBOTT: Yes, that is correct. We have excluded farmers and fishermen, but perhaps a good case could be made out for single real estate investors.

Hon. Mr. FRASER: On the point of the depreciation of equipment, take, for instance, a crane that cost the owner $40,000. Let us say that he depreciates the crane in two years to the extent of $20,000 and he sells the crane for $40,000. I understand that the depreciation is then charged back to the income.

Hon. Mr. ABBOTT: Yes, and if he buys a new crane for $40,000 he stands about exactly in the same place. What I want to point out is that he has written off, say $10,000 on the crane, and he sells it for the purchase price. The $10,000 is then returned to taxable income. Is that correct?

Hon. Mr. HAYDEN: That is right unless he has other assets.

Hon. Mr. ABBOTT: Unless he buys a new one.

Hon. Mr. FRASER: If he does not buy a new one the $10,000 goes back into his earning account.

Hon. Mr. ABBOTT: Yes.

Hon. Mr. FRASER: Under our present rates of taxation he has only taken advantage of 40 per cent for taxation purposes. The other 60 per cent has been a capital investment of tax-paid funds of his own. Then you come along and charge this 40 per cent to the taxable income.

Hon. Mr. ABBOTT: We take out at the same rate we put back in. It must be remembered that on the other side of the picture, if he sells the crane for less than his depreciated value, he can charge that in against the profits. It he is under-depreciated, he gets the benefit of his under-depreciation.

Hon. Mr. FRASER: I find that companies and their auditors figure that when they write off twenty or forty per cent depreciation they have escaped taxation on the whole amount, instead of realizing the fact that they have invested their own tax paid funds. So that when you charge back the $10,000 into your taxable income, you are again taxed 40 per cent.

Hon. Mr. ABBOTT: You are taxed at the same rate that you put back in. In other words, there is no equity.

Hon. Mr. HAYDEN: A question arises in dealing with insurance. Supposing a rented house is totally destroyed by fire. In that case the ordinary provision here applies. What I was going to suggest was this. Supposing the person wanted to rebuild. If he had his insurance on an appraisal value he would be getting more in insurance than the depreciated value of the property at that moment. But when you applied your new depreciation rule you would leave him with less than the total amount that it would cost him to rebuild.

Hon. Mr. ABBOTT: If, as may well happen, I decide that it is appropriate to exclude investors in real estate from the operation of that rule which is primarily intended for fluctuating business operations, your point would be answered.

Hon. Mr. HAYDEN: But business people could be affected by it too. The suggestion I would like to have considered is this: if a man were left with the proceeds of the insurance and showed an intention to rebuild within a reasonable time, you would accomplish the same result if you said that the capital value of the new asset that he built would start off at the depreciated value of the old building at the time it was destroyed by fire. In that way he would be left with enough money to rebuild and it would not be necessary for property owners to carry increased insurance to cover any tax on the proceeds of insurance policies.

Hon. Mr. ABBOTT: I would have to think that out.

Hon. Mr. NICOL: Insurance policies in our province contain a statutory condition that the insurance company may rebuild instead of paying money over to the insured.

Hon. Mr. HAYDEN: What happens if the insurance company rebuilds the property?

Hon. Mr. ABBOTT: I take it, Senator Nicol, that the kind of case you have in mind is where a man collects $25,000, say, because a building has been completely destroyed by fire.

Hon. Mr. NICOL: No. Say a property valued at $20,000 is damaged by fire to the extent of $10,000 but the owner wants the insurance company to pay $15,000. The insurance company may say that instead of paying him $15,000 it will rebuild the damaged portion.

Hon. Mr. ABBOTT: In that case he does not receive any money but simply is given his building back.

Hon. Mr. NICOL: Yes. Let us assume that is done in 1950 and afterwards the property is depreciated.

Hon. Mr. ABBOTT: If the insurance company repaired and reconstructed the property I should think that under the operation of the new principle he would be in exactly the same position as before the fire, and his asset account would stand exactly as it did before.

Hon. Mr. HAYDEN: What would happen if the property were completely destroyed?

The CHAIRMAN: The case of a partial loss is covered but the case of total loss is not covered, is that the point?

Hon. Mr. HAYDEN: That is it.

Hon. Mr. ABBOTT: If the money is required to rebuild the asset, the cost of rebuilding is charged right into the asset account. That, I take it, is one of the things that have to be spelled out in the regulations. If you have underpreciated your property and you get from the insurance company $10,000 more than your depreciated value, you add that $10,000 or charge it back from your depreciation account and take it into profit. Then if you rebuild the same building and it costs you twice as much, you charge the extra cost or whatever the cost is back in and you offset the $10,000 that you have taken out of depreciation and put it into profit and loss.

Hon. Mr. HAYDEN: That sounds all right, but it does not work out that way. Take a look at paragraph (*c*) (iii), on page 6. It says: "Proceeds of disposition of property include an amount payable under a policy of insurance in respect of loss or destruction of property". That simply means that if I have a property insured for $15,000 and it is totally destroyed, and the depreciated value at the time of the fire was $10,000, then some part of the proceeds is going to come back into my income for the year.

Hon. Mr. ABBOTT: If the amount that you use to rebuild exceeds the depreciated value of your old asset you can charge that back into the account.

Hon. Mr. HAYDEN: Where does it say that?

Hon. Mr. ABBOTT: That is the way it works out on a sound accounting basis.

Hon. Mr. HAYDEN: That is not what the section says.

Hon. Mr. ABBOTT: The section does not spell out the accounting practices.

Hon. Mr. HAYDEN: But it does spell out the regulation in the case of a property that is partially destroyed, and it is just as necessary to have it spelled out in the case of a property that is completely destroyed.

Hon. Mr. ABBOTT: Perhaps Mr. Gavsie can answer your question.

Mr. GAVSIE: If a property is destroyed this year and the owner rebuilds, in the meantime he has got some money from the insurance company. Well, the old and the new property are of the same class, so that the insurance proceeds would go under the same fund that the new property was charged to and in effect they would be offset. There would be nothing charged back to income if the new property cost more than the amount he got from the insurance company.

Hon. Mr. ABBOTT: Would you explain why we need a separate provision for the cost of repairs?

Hon. Mr. HAYDEN: You have made the assumption that the new property costs more than the amount of money received from the insurance company. That is not the point.

Mr. GAVSIE: I thought it was.

Hon. Mr. CAMPBELL: Mr. Chairman, I move that we adjourn till 2 o'clock.

Hon. Mr. ABBOTT: I would ask to be excused from attending at 2 o'clock, for there is a cabinet meeting at that time. I may say there are two things that I shall be very glad to consider. The first is the possible amendment suggested by

Senator Vien, that greater latitude be given as to where depreciation might be spread forward; and the other—and I may say that I am strongly impressed with the argument on that—is that revenue producing real estate should be excluded from the operation of the new basis for depreciation.

Hon. Mr. NICOL: That is, with respect to the small property owner?

Hon. Mr. ABBOTT: I would be inclined to go all the way and exclude all such real estate, because I think the principle would be the same regardless of the value of the property.

Hon. Mr. NICOL: Senator Moraud has in mind the small property owner.

Hon. Mr. ABBOTT: Any amendment which might be considered desirable to make could wait until the spring of 1950, because the recapture provision will not really operate for a year. I should like to consider whether the principle should be restricted to the small owner only or be extended to cover all owners, or to neither. I should not like to make a snap judgment on it at this moment.

Hon. Mr. CAMPBELL: I understand this legislation has been under study now for well over a year.

Hon. Mr. ABBOTT: That is right.

Hon. Mr. CAMPBELL: And that it has been carefully considered by the departments concerned and is a matter of top financial policy of the government. It is a matter of top financial policy of the government.

Hon. Mr. ABBOTT: I do not think there is any question about that. If I may speak personally, I would say that I do not think I can backtrack on this new piece of depreciation legislation. I have been a couple of years drafting and bringing in a new income tax act, and I have acknowledged publicly that we have a better system of depreciation. So far as I am concerned, I am going to stick to it. I am quite willing to make exceptions when it is demonstrated to me that for special classes of property it would be better to operate under the old system; but, certainly I am not going back on this new system until I get better evidence than I have heard so far.

I have had Fred Johnston, President of the Bell Telephone Company, in to see me. As you know, the telephone company is very much interested in depreciation rates. We discussed this whole question, and he talked it over with the Department of National Revenue, and I have had no serious criticism of the new changes—certainly nothing like that of rent control.

Hon. Mr. LAMBERT: There has been no question of the high policy of the government, to put this through.

Hon. Mr. ABBOTT: No.

The CHAIRMAN: The motion is that the committee now rise until 2 o'clock.

At 1.10 p.m. the committee adjourned until 2 p.m.

On resuming:

The CHAIRMAN: Gentlemen, we have a quorum, so will you please come to order. Have we reached a point where we can attack the bill clause by clause? I should think if there are any questions they can be brought up under particular headings.

Hon. Mr. HAYDEN: I asked a question this morning that I think perhaps Mr. Gavsie is prepared to answer now.

The CHAIRMAN: Could we deal with it when we come to sections 7 and 8?

Hon. Mr. HAYDEN: It would fit in at that time all right.

On section 1—"income from office or employment".

The CHAIRMAN: I do not think it is necessary to read the section through.

Hon. Mr. HAYDEN: No, I think it is a remedial section and will be very welcome to some people. It increases the exceptions from the general rule of having to include everything in income. I think the same applies to the whole section.

Section 1 was agreed to.

On section 2 (1)—"loan to shareholder".

Hon. Mr. CAMPBELL: Paragraph (*c*) adds the words "from the corporation". The purpose of the paragraph is to prevent a person from using the surpluses of a corporation to buy out the interests of the majority shareholders. The section, as originally intended, was to induce officers or servants of a corporation to buy shares of capital stock from the corporation.

Hon. Mr. HUGESSEN: That is unissued shares?

The CHAIRMAN: Treasury shares.

Hon. Mr. CAMPBELL: Yes.

The CHAIRMAN: Subsection 2 of that section refers to the time with respect to the application to loans.

Section 2 was agreed to.

On section 3—"exceptions".

The CHAIRMAN: This is a relieving section.

Hon. Mr. HAYDEN: It goes back into the Income War Tax Act, but as it is a relieving section, it is all right.

Section 3 was agreed to.

On Section 4—"deductions allowed".

Hon. Mr. VIEN: Will you explain that section, Mr. Chairman?

The CHAIRMAN: This is a long section dealing with allowable deductions. the first part of which I notice deals with a provision which was announced about budgets some time last year, changing a practice which had been in for a short time of charging clergymen in respect of the rental cost of their residence. That provision is contained in subsection 2.

Hon. Mr. HAYDEN: I think it goes so far as to apply to clergymen who actually own the place in which they live. The subsection is remedial.

Section 4 (1) and (2) were agreed to.

The CHAIRMAN: Subsection 3 deals with lessee's shares.

Mr. GAVSIE: That is just a correction in legislation. The legislation, by error, referred to "section" instead of "subsection". There is no change otherwise.

Section 4 (3) was agreed to.

The CHAIRMAN: On section 4 (4)—"banks".

Hon. Mr. MORAUD: That is all right.

Hon. Mr. HAYDEN: You will correct the error in printing, where it says "blank".

Section 4 (4) was agreed to.

On section 4 (5)—"relieving telegrapher's and station agent's expenses".

Section 4 (5) was agreed to.

On section 4 (6)—"salesmen".

The CHAIRMAN: Subsection 6 deals with the expenses of salesmen.

Hon. Mr. HAYDEN: Well, the new part is (*d*), is it not?

The CHAIRMAN: And if he was not in receipt of an allowance for travelling expenses.

Mr. GAVSIE: If he was in receipt of an allowance he need not take it in his income.

Hon. Mr. HAYDEN: In other words, if he is on straight commission he gets expenses, if he is not on straight commission he gets the allowance.

Mr. GAVSIE: The allowance is not income, by virtue of the amendment in clause 1. If it is not income he is not to deduct it from his earnings. He cannot have it twice. He cannot have it excluded from income and then deduct it from his other income. That is the purpose of that paragraph.

The CHAIRMAN: In other words, he cannot get the allowance and the actual expenses as well.

Mr. GAVSIE: Yes.

Subsection (6) agreed to.

On subsection (7):

The CHAIRMAN: I think that is all right too.

Dr. EATON: It is simply a technical change in the preamble.

Subsection (7) agreed to.

On subsection (4):

The CHAIRMAN: This subsection makes it applicable to 1949 and subsequent years.

Subsection (4) agreed to.

On section 5—deductions allowed.

The CHAIRMAN: This also deals with deductions. It makes the amendment affecting clergymen applicable to 1948.

Section 5 was agreed to.

On section 6—inadequate considerations.

The CHAIRMAN: Section 6 deals with transactions between persons at arm's length for inadequate consideration.

Hon. Mr. HAYDEN: What the dickens is "not at arm's length"? I can understand the expression sometimes.

The CHAIRMAN: It is defined in the present act.

Hon. Mr. CAMPBELL: This section is intended just to complete the old section by providing that in the event of the rent being lesser than the normal amount—

Mr. GAVSIE: What you have in section 17 now is a sale or a purchase. The other was a lease one way. This is a lease the other way.

Hon. Mr. HAYDEN: You have got to push them the full arm's length away from you. You are strangers once you do that.

Hon. Mr. MACLENNAN: Arm's length has a legal significance.

Hon. Mr. HAYDEN: That is right.

Section 6 was agreed to.

On section 7—depreciation (etcetera).

The CHAIRMAN: Do you want to deal with sections 7 and 8 now?

Hon. Mr. HAYDEN: We may as well, because we run into the effect of them in other sections. Why should we not go right through?

The CHAIRMAN: All right: section 7, subsection (1). We are dealing with the whole section, subsections (1) to (6).

Hon. Mr. VIEN: Have you considered the possibility of adding after subsection (1), "or otherwise as provided by regulation"?

Hon. Mr. HAYDEN: The minister said he would deal with that. He wanted some time to consider it, but the idea was that it would still be time enough when the budget comes down.

Hon. Mr. VIEN: Could not you drop the words, "shall be included in computing his income"?

Hon. Mr. HAYDEN: I don't think you could do that.

Mr. GAVSIE: You would have to have some rules. The difficulty about adding regulations is that primarily the years to which this income should be related should be in the statute. If you make a regulation immediately you have the question of interest, and there are several other questions involved. That is why I think the minister suggested he would consider it and come up with something that would be applicable, and make it retroactive.

Hon. Mr. HAYDEN: To avoid the question of interest.

The CHAIRMAN: I think the danger is, if you related that back to the years in which the depreciation was accumulated, you would automatically incur interest charges for the same period.

Hon. Mr. HAYDEN: I raised this question earlier, and I am perfectly satisfied with the minister's statement that he will give consideration to it. He knows what the problem is, and I think we will get some relief.

Hon. Mr. ROBERTSON: I might say that I asked him for his instructions just before he left the meeting, and he said that the point that we brought up in this regard, and as to real estate generally, he would give very serious consideration to.

Hon. Mr. MORAUD: When? Now?

Hon. Mr. ROBERTSON: No, next session.

Hon. Mr. NICOL: I made a motion this morning. I would beg leave to withdraw my motion at the present time.

The CHAIRMAN: Thank you, senator. Shall subsection (1) carry? Carried. Now, subsection (2).

Hon. Mr. HAYDEN: I wanted to ask a question on subsection (2). If you have a series of transactions, a series of sales of property, and in one of those sales only the parties were not at arm's length in accordance with the statute, then when you got down to about the fourth purchaser, and the one who was not at arm's length was about the second one, how is that going to affect the value for depreciation purposes in the case of the last man in the line?

Mr. GAVSIE: This rule would only apply as between the two people that were not at arm's length. When it passes out of the hands of the recipient not at arm's length, then it is in the open again.

Hon. Mr. HAYDEN: Then the subsequent purchaser for whatever the cost was, without being a party to or having knowledge of the fact that the earlier relationship of vendor and purchaser at that time was not at arm's length, would not be affected at all?

Mr. GAVSIE: No.

Subsection (2) was agreed to.

The CHAIRMAN: Subsection (3) defines "depreciable property of a taxpayer" "disposition of property", "proceeds of disposition", "total depreciation allowed to a taxpayer", and also defines "undepreciated capital cost to a taxpayer of depreciable property."

Hon. Mr. HAYDEN: I want to ask a question under subsection (3) and also (*c*), (iii). It has to do with where property was fully insured and totally destroyed. My understanding in discussing the matter with Mr. Gavsie is that, in taking accounts at the end of the year in those circumstances, if

the replacement property could be constructed with the full proceeds of the insurance, that could be done and the only effect would be that the value of that property when it had been replaced would be the balance of the depreciated value of the property that had been destroyed. It would start off there as though there had not been a fire.

Mr. GAVSIE: That is right.

Hon. Mr. HAYDEN: Then there would be no taking away physically from the owner of the property of any part of the proceeds of the insurance so as to leave him with less than 100 per cent physically.

The CHAIRMAN: Unless there was further capital added to get a more valuable property.

Hon. Mr. HAYDEN: Oh, yes. Then, that would add to the capital cost.

The CHAIRMAN: To your assets.

Hon. Mr. HAYDEN: If any doubt arises as to your authority to interpret in that fashion under the section—?

Mr. GAVSIE: Then we will be back for an amendment.

Subsection (*c*) was agreed to.

Hon. Mr. HAYDEN: What is meant by the statement in subsection (*d*) "before any time"? It says "total depreciation allowed to a taxpayer before any time."

Mr. GAVSIE: You want to know what the depreciation is before that time. Sometimes it is at the commencement of the year and other times it is at the end of the year. We have to define it in relation to a period of time, that the total depreciation allowed to a taxpayer before the commencement of the year is so-and-so, and at the end of the year—

Hon. Mr. HAYDEN: It reads very oddly.

Mr. GAVSIE: There was a lot of struggling with it, and it was done in this instance because, once you have your pencil out, you can follow it much easier. Sometimes you have to use what in effect is a formula to express the meaning. I was wondering whether it meant "as of any time" because you use those words in the next paragraph.

Mr. GAVSIE: We also use the words "before that time".

Hon. Mr. HAYDEN: All right, if you need that language in there.

Paragraphs (*d*) and (*e*) were agreed to.

The CHAIRMAN: Under subsection 4 there are a series of rules.

Hon. Mr. HAYDEN: What is the meaning of "some other purpose"?

Mr. GAVSIE: Well, if it is for personal use as distinct from using it for the purpose of earning income.

Hon. Mr. HAYDEN: There are two classes. If I acquire property for investment income purposes or acquire property to earn income out of a business, and if I switch to some other class for some other purpose, I mark time and take a fair value, and it is the same as a sale.

Mr. GAVSIE: That is right.

Hon. Mr. HAYDEN: Suppose I switch my business from manufacturing washing machines to manufacturing radios, am I regarded as having switched my business to "some other purpose"?

Mr. GAVSIE: There is no change as long as it is for your own business purposes. If a new company is incorporated to start a radio business under a new name, that is different.

Hon. Mr. CAMPBELL: Is this not the meaning? If you have a property which you are using for a business for the purpose of gaining a profit, you can

change the nature of that business without running contrary to this statute? However, if you have a boat which you have been using for revenue purposes and you change it into a yacht, that is different.

Hon. Mr. HAYDEN: What about the use of the words "a business"?

The CHAIRMAN: It does not say "any business".

Mr. GAVSIE: That is just a term of art that is used all through the bill. I am told that if you are manufacturing radios one day and the next day you are manufacturing washing machines, it is still the same business. It is only where there is a change of corporation and name that this section takes effect.

Hon. Mr. NICOL: If you are manufacturing washing machines and you sell your business to a new corporation for the purpose of manufacturing radios, then this law comes into effect.

Mr. GAVSIE: Yes, because there is a change of taxpayers. A new taxpayer has bought the assets and the new company, being a separate corporate entity, would be regarded as a new taxpayer.

The CHAIRMAN: Shall 4 (*a*) carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Then we come to paragraph (*b*).

Mr. GAVSIE: That is the reverse. The person acquires property as a personal residence and then decides to rent it for the purpose of gaining income therefrom.

Hon. Mr. HAYDEN: This is asking a person to use his imagination a great deal. How did I acquire a property for some other purpose if I have not acquired it for any purpose? I first have to acquire it for some purpose.

The CHAIRMAN: What it means is where a taxpayer uses a property for the purpose of gaining income, that he formerly acquired for another purpose.

Hon. Mr. HAYDEN: Paragraph (*b*) says, "where a taxpayer, having acquired property for some other purpose, has commenced at a later time to use it for the purpose of gaining or producing income . . ."

The CHAIRMAN: I do not see why the draftsmen thought it necessary to put this in backwards.

Hon. Mr. HAYDEN: That is my point. I think it is in backwards.

Mr. GAVSIE: We know that under paragraph (*a*) the taxpayer has acquired the property for the purpose of gaining income or for producing income from a business, and later he uses it for some other purpose. We know what the "some other purpose" is for personal use.

Hon. Mr. HAYDEN: Where does it say "personal"?

Mr. GAVSIE: Well, it may actually be for his family and not himself.

Hon. Mr. HAYDEN: I see, this has to be written on a high level of language.

Mr. GAVSIE: Yes.

Hon. Mr. MACLENNAN: And they have to be sure to carry on the obscurity.

Some Hon. SENATORS: Oh, oh.

The CHAIRMAN: Does it contemplate that during its use for some other purpose it will become depreciable?

Mr. GAVSIE: No, because the property has been held for a purpose for which no depreciation can be charged.

Hon. Mr. HAYDEN: There would be the simplified way of expressing it. You have just done it now. That would be ordinary intelligible English.

The CHAIRMAN: Let us take the case of a property purchased for a non-depreciable purpose, and you subsequently decide in a year or so to use it in a business. You have not depreciated it in the two years that you had it for a non-business purpose, and you decide to use it for your business. Should this total capital cost not come in?

Hon. Mr. HAYDEN: Well, it might have a higher fair market value at the time he turns it in.

Mr. GAVSIE: Yes.

The CHAIRMAN: Shall paragraph (*b*) carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Now we come to paragraph (*c*).

Hon. Mr. HUGESSEN: That seems to me to be the answer to the question raised this morning by Senators Vien and DuTremblay.

Hon. Mr. HAYDEN: No, because this is where a taxpayer has acquired property by gift, bequest or inheritance. They were dealing with situations where the executor was selling in the course of administration. This is a different situation.

Hon. Mr. HUGESSEN: From an executor selling property?

Hon. Mr. HAYDEN: Yes. The executor would be making a sale in the course of administration.

The CHAIRMAN: This would apply to the heir of the estate?

Hon. Mr. HAYDEN: Yes.

Mr. GAVSIE: There might be love and affection and reasons giving rise to the property being bequeather. He cannot establish by cheque that he has paid so many dollars for the property, but he can nevertheless depreciate it at fair market value.

Hon. Mr. HUGESSEN: And the depreciation taken by the deceased goes out the window?

Mr. GAVSIE: Yes.

Hon. Mr. HAYDEN: That is why I am all in favour of it.

The CHAIRMAN: Shall this paragraph carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: We come now to paragraph (*d*).

Hon. Mr. HAYDEN: This is the reverse. This means that if I have depreciable assets in my hands and I give it away otherwise than by will, I shall be deemed to have disposed of it at the time as a gift at its fair market value.

Otherwise there is a wide-open door if the person sells and is obliged to bring in any depreciation that he may have recovered.

Hon. Mr. HAYDEN: If I make a gift gratis of a depreciable asset to some person, in my lifetime, you say that so far as I am concerned the fair market value of the asset is to be determined at that time, but if the fair market value is at least equal to my capital cost as at January 1, 1949, the recapture provision will apply to any depreciation that I have taken?

Mr. GAVSIE: Yes, and the donee sets up the property at fair market value for depreciation.

Hon. Mr. VIEN: But why should the donor be obliged to add to his taxable income the difference between the purchase price, as set out on the 1st of January, 1949, and the market value at the time he gave the property away?

Hon. Mr. HAYDEN: After all, what is given is the depreciated capital value of the property. Why should not the asset in the hands of the recipient carry a capital value equal to the depreciated value at the time of the gift? Why should a man have to pay a tax on some part of the depreciation? Why not have the continuity of the depreciation preserved?

Hon. Mr. NICOL: If your suggestion were followed it would defeat the object of the law. If a man sells a property he has to pay a tax, so why should he not have to pay a tax if he gives the property away?

Dr. EATON: Or why should he not be allowed to take advantage of the loss if the market value is below the depreciated value?

Hon. Mr. HAYDEN: Why should he not have the option?

Dr. EATON: But a principle is established.

Hon. Mr. HAYDEN: The man who makes a voluntary gift runs the risk of having to pay income tax on the amount of depreciation that you recapture.

Mr. GAVSIE: Once certain rules are made to apply in the case of a sale, I think it is fair they should apply when there is a gift. There is, of course, no recapture where property is transferred by a will.

Hon. Mr. VIEN: How would you establish the fair market value? Would you require the donor or the donee to establish to your satisfaction what the fair market value was at the time of the gift?

Mr. GAVSIE: It does not make a great deal of difference to the department, senator, because the donor is deemed to have received the fair market value and the donee is deemed to have paid it to him, because the donee will be depreciating the same amount as the donor is deemed to have received. So far as the department is concerned there is no difference, unless one party is not a taxpayer and the other is a substantial taxpayer.

Hon. Mr. NICOL: The donor has to pay a gift tax, and in order to determine what the gift tax is the property must be valued.

Hon. Mr. HAYDEN: The difficulty is that two taxes have to be paid. First of all, the man who gives away a piece of property in his lifetime is obliged, if the value of the property exceeds a certain amount, to pay gift tax, and also the depreciation that he has taken on the property can be recaptured. Under the present law a man pays a gift tax, but this amendment proposes an additional tax.

Hon. Mr. CAMPBELL: Mr. Chairman, is it not the object of this to prevent a person from defeating the whole purpose of the act? If a man sold a piece of property for $X, which would make him liable to a certain tax on recaptured depreciation, he could in the absence of such a provision as this defeat the whole purpose of the legislation.

Hon. Mr. HAYDEN: It is an exaggeration to say that he could defeat the whole purpose of the legislation for whether this provision is in the law or not the man would be subject to the full force and effect of the law.

Mr. GAVSIE: I do not think Senator Campbell meant that the full purpose of the legislation would be defeated, but that this would be an obvious omission.

Hon. Mr. CAMPBELL: Yes.

Hon. Mr. HAYDEN: The scheme of depreciation is to recapture depreciation or to see to it that if it is not recaptured the value for depreciation in the next hands will not be carried at a higher figure than the depreciated value before the transfer.

Mr. GAVSIE: No, we go further than that. What we are seeking to provide is that when a person disposes of property, whether by gift or by sale, the fair market value will be taken into consideration, both for the purpose of sale and for the purpose of purchase. In cases where there is a deal between strangers we assume that what a stranger is prepared to pay for a property is the fair market value, but where there is a gift we have no such assumption as that.

Hon. Mr. HAYDEN: Suppose a philanthropic citizen owned an industrial site and some buildings on it and decided to give the whole thing away to an organization that he set up for charitable purposes. Not only would he be giving away the property, but if it had been depreciated before he made the gift he would also have to pay tax on the recaptured depreciation to the extent of the fair market value.

The CHAIRMAN: If the fair market value exceed the depreciated value.

Hon. Mr. HAYDEN: Yes. It has a lot of implications.

Dr. EATON: If it was valued at more than that he has had something that he was not entitled to.

Hon. Mr. HAYDEN: No, he has not had anything. He has not sold the property nor has he given it to any person who would realize a gain on it, but he has made a gift to an organization for charitable purposes.

Mr. GAVSIE: He would be giving an amount equivalent to the fair market market value of the property. That is what he would claim as a charitable deduction; he certainly would not claim the depreciated value. Suppose the property stood on his books at $1, he would not claim that that was the value.

Hon. Mr. DUTREMBLAY: Under this new scheme, if a man sells a property at a profit, he is taxed on that as if it were ordinary revenue.

Mr. GAVSIE: No, only to the extent that he has claimed allowances under the Act since 1949.

Hon. Mr. CAMPBELL: I move that paragraph (*e*) be carried.

Mr. GAVSIE: This refers to the case of a doctor's office; in other words, part of his home is used for personal purposes and part for business.

Hon. Mr. HAYDEN: Is it not the practice now to depreciate in relation to the property used for carrying on business?

Mr. GAVSIE: Yes.

Hon. Mr. DUTREMBLAY: I did not quite understand your answer to my question.

Mr. GAVSIE: Supposing a property cost $100, and the owner took allowances since 1949 of $50, leaving a balance of $50. He then sells the property at $150; it cost him $100, and $50 is capital profit. We do not touch that. We look at the amount to see how much allowance he has taken since 1949, and it turns out in this case to be $50.

Hon. Mr. VIEN: That is deducted.

Mr. GAVSIE: That is put in the group, if there is a group; it is the allowance he has taken. If he has taken no allowance then there is nothing to write back. In the illustration I gave the property cost $100, and if the owner chose not to take any allowance, and then sells the property, there is nothing to write back.

Hon. Mr. DUTREMBLAY: Under the present regulations, if he took the allowance, he would keep the profit just the same.

Mr. GAVSIE: That is right; that is the change. He now brings it back, but before if the property cost him $100, and he took an allowance of $50, there was $50 remaining after depreciation. Now, should he have to sell the property for $25, under previous legislation he would suffer a capital loss of $25 for which he could get no relief tax-wise. Under this provision, if he were to sell the property for $25 he would have a loss of $25 which he could recover. On the one hand you pick up what you have taken, and on the other hand provision is made for recovery of what you have not taken.

Hon. Mr. CAMPBELL: I move that paragraph (*e*) be carried.

Hon. Mr. VIEN: Is this scheme in operation elsewhere?

Hon. Mr. HAYDEN: Yes, in England.

The CHAIRMAN: Paragraph (*e*) carried.

We now come to paragraph (*f*).

Hon. Mr. HAYDEN: Here we have a change in the language; it says "for other purposes". Why should it not read "for some other purpose" if there is some charm in that connotation; here it was apparently decided to throw it overboard.

I thought the conditions were, first, for the purpose of gaining income from a property, and second, producing income through a business, with a third category "for some other purpose".

Hon. Mr. MacLennan: You are getting sardonic.

Hon. Mr. Hayden: We know the meaning of it now—it means personal.

The Chairman: There isn't much doubt about that; it was a little broader perhaps.

Hon. Mr. Hayden: If, "for some other purpose" has some special significance, and that is what is meant in this paragraph, then let us keep it.

The Chairman: If there is any difference in the meaning.

Hon. Mr. Hayden: I do not know whether or not there is, but it indicates a plural, and I understood there were three categories: gaining income, producing income, and as a third category, for some other purpose.

Hon. Mr. Campbell: Is not the plural correct in that case?

Hon. Mr. Hayden: I do not know. If it is, then it should be all plural.

Hon. Mr. Stevenson: What is the difference between "for some purpose" and "for other purposes"?

Hon. Mr. Hayden: I do not know.

Hon. Mr. Campbell: I move the section carried.

The Chairman: I declare paragraph (*f*) carried.

Hon. Mr. Hayden: Referring to this paragraph (*h*) I don't know whether Dr. Eaton or Mr. Gavsie can answer this, but I take it that any subsidy or assistance that might be received in connection with a property, whether it is from the federal authority or from the provincial authority or a municipality, would be a deduction from the capital cost of that property for depreciation purposes.

The Chairman: I think Mr. Gavsie will tell you that that is the situation at the moment. There is no change. You cannot write off a grant or subsidy.

Hon. Mr. McLean: What about drydocks which get a subsidy for carrying on business?

The Chairman: You cannot set up a subsidy as part of the cost of your property to be depreciated.

Hon. Mr. Hayden: It says "in respect of or for the acquisition of property". It may be in respect of property or for the acquisition of property. "In respect of property" might very well be during the period of operation.

Hon. Mr. McLean: Between wars we subsidize drydocks right along to keep them in business.

Mr. Gavsie: That subsidy was not for the building of a drydock.

Hon. Mr. McLean: They may use the subsidy to retire bonds.

Mr. Gavsie: Yes, I was going to say, to pay the interest and take care of the sinking fund.

Hon. Mr. McLean: I am not interested in any drydocks, but I know that it is very hard to make them pay between wars.

Mr. Gavsie: Those are under the Drydock Subsidies Act, which was passed in 1908, long before income tax.

Hon. Mr. Hayden: Certainly, if in their bookkeeping and their financial statements they do not include that subsidy as part of the capital cost, there is no problem under (*h*).

Hon. Mr. VIEN: Except this, that if a provincial government or a municipality gives a subsidy to help a new industry, why should you take away this assistance by deducting from the value of the property the donation that they may have received?

The CHAIRMAN: You are not taking it away, senator. As I understand it, you are simply putting it in the category that the taxpayer cannot recover it again, as he could his own capital invested. In other words, in setting up the value of the building, if he had a provincial subsidy of $10,000 and he put in $40,000 of his own money, the capital cost of the property to him would be the $40,000 which he could recover by way of depreciation.

Hon. Mr. VIEN: But if a company is organized for, let us say, the purpose of creating a water-works in a municipality, or an aqueduct, or a sewerage system—these are disappearing, but there are some of that character still persisting in some parts—

The CHAIRMAN: You mean, a private company?

Hon. Mr. VIEN: Then he gets his subsidy towards the purpose for which the company is organized. Property is then bought. Are you going to push it through into the property that he is buying?

Mr. GAVSIE: No. It is a case where they are building the aqueduct and they get a contribution from the municipality. The aqueduct is costing a million dollars. They get a contribution of $10,000, then what they depreciate is $990,000. That is all that means. There is no attempt to recover the amount. Their cost is $990,000.

Hon. Mr. HAYDEN: I move that we adjourn until the Senate rises.

Hon. Mr. CAMPBELL: Would it be in order to suggest to the leader that the house meet and adjourn during pleasure, and then we could proceed with this matter and probably dispose of it?

The CHAIRMAN: The understanding I had with the leader of the government was that we would rise now to meet again this afternoon when the Senate rises, and I think perhaps it would upset things too much if we endeavoured at this stage to make a change.

Hon. Mr. VIEN: I move that we rise now, to resume later today.

The CHAIRMAN: Is that agreed to? Carried.

(The committee resumed its hearing.)

The CHAIRMAN: Honourable senators, I think we got down to subsection 4 at the top of page 8 of the bill. Shall subsection 4 carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Then we come to subsection 5, which defines "business". Shall subsection 5 carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Next is subsection 6. Does this section carry?

Hon. Mr. HAYDEN: Is there an amendment there?

The CHAIRMAN: Yes. The amendment provides for a new subsection 6 which reads as follows:

> Subsection (1) does not apply in determining income from farming or fishing.

Does this subsection carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Then there is subsection 2 of section 7 which reads as follows:

> This section is applicable to the 1949 and subsequent taxation years.

Hon. Mr. HAYDEN: What applies in the case of farming and fishing?

The CHAIRMAN: Section 11, 1 (*a*) of the Income Tax Act is not affected, which is the general section saying that you may recover capital in accordance with the regulations.

Hon. Mr. HAYDEN: The only regulations that are going to be made, are the ones under this bill. Are they going to be made in connection with farmers and fishermen separately?

Hon. Mr. McLEAN: What about the case cited this morning, of a farmer who bought an engine?

Mr. GAVSIE: He will not be able to get the write off.

Hon. Mr. McLEAN: Why, then, were we given this example?

Mr. GAVSIE: I think Mr. Abbott said that if these new regulations were not going to be applicable he would not get the benefit.

Hon. Mr. NICOL: What person or persons come under the definition of "a fisherman"? For instance, is the person who fishes for whales considered a fisherman?

Mr. GAVSIE: I think the terms are defined in the Act.

Hon. Mr. McLEAN: What about fishing companies?

Mr. GAVSIE: A company may have income from several sources, and the part of the income that relates to fishing would be governed by the regulations that will have to be made in respect to fishing.

Hon. Mr. HAYDEN: Fishing is defined at section 127, subsection 1 (*t*) of the Income Tax Act.

Hon. Mr. NICOL: What is a fisherman? We have large operators who fish and can their product. Are they called fishermen?

The CHAIRMAN: The definition of a fisherman as given in section 127 of the Act is as follows:

> "Fishing" includes fishing for or catching shellfish, crustaceans, and marine animals but does not include an office or employment under a person engaged in the business of fishing.

That is a marine animal, I suppose.

Hon. Mr. HAYDEN: So it only covers the men who are actually engaged in the act of catching this fish.

The CHAIRMAN: "fishing for or catching". Now, farming is defined in subsection 1, paragraph (*o*) of the same section 127:

> "Farming" includes tillage of the soil, livestock raising, raising of poultry, fur farming, dairying, fruit growing and the keeping of bees but does not include an office or employment under a person engaged in the business of a farming.

I take it that that is the employee of a farmer.

Mr. GAVSIE: That is a hired man.

Hon. Mr. NICOL: And it would include a gentleman farmer.

Hon. Mr. HAYDEN: It does not include the hired man.

Mr. GAVSIE: That is right; it excludes the hired man.

The CHAIRMAN: It is the occupation of farming or fishing; it is not merely an individual. Does subsection (2) carry?

Some Hon. SENATORS: Carried.

On section 8—transitional provisions *re* depreciation.

The CHAIRMAN: Subsection 1 of section 8 sets out that "where a taxpayer has acquired depreciable property before the commencement of the 1949 taxation year, the following rules are applicable for the purpose of section 20 of the Income Tax Act and regulations made under paragraph (*a*) of subsection 1 of section 11 of the Income Tax Act". Then it goes on, but I do not know whether you want me to read it or not.

Hon. Mr. HAYDEN: Could we have a typical example given to it by Dr. Eaton or Mr. Gavsie?

Mr. GAVSIE: What paragraph (*a*) says is that for the purposes of arriving at the 1949 cost you take the original cost—this is of an asset bought before 1949—and you take the original cost and you deduct from that the total amount of depreciation which has been allowed for capital in accordance with the previous practice; and any special or extra depreciation that was allowed, and one-half of the double depreciation, as well as any depreciation that was in existence in 1917—assuming that you are dealing with assets that were acquired before 1917. So, for arriving at the 1948 costs you take these original costs less all the depreciation that has been accumulated since the date of acquisition.

Hon. Mr. MCLEAN: What about special depreciation that was set up for taxes paid on it? I do not mean the ordinary depreciations allowed, but special depreciations set up and taxes paid on it.

Mr. GAVSIE: You got the special depreciation which has the effect of reducing the amount of tax which you would otherwise pay. Under the old law there was provision that if you sold the asset in respect of which you got special depreciation your assessments would be re-opened and your depreciation that you took in those years would be reduced down to normal depreciation, which would have the effect of increasing your taxable income for those years and you would get a new assessment for those years and you would have to pay that plus the interest. The way the new system will operate is that this special depreciation which you received in the years prior to 1949, shall be deemed to have been allowed to the taxpayer in 1949. Therefore, under this new system, if the assets are subsequently sold, there will not be any reopening of the assessments prior to 1949, but they will be reflected in the same way as normal depreciation will be taken after 1949.

Hon. Mr. CAMPBELL: In other words, they are recaptured for tax purposes?

Mr. GAVSIE: That is right. Under the old system you re-opened the assessment under which you took it, and that was a liability for those years which immediately created in addition to the tax liability, a liability for interest.

Hon. Mr. HAYDEN: I understand your explanation, but would you look for a moment at section 8, paragraph (*a*) (ii) where it states "The total amount of depreciation for such of the said property as he had at the commencement of that year that, since the commencement of 1917, has been or should have been taken into account in accordance with the practice of the Department of National Revenue, in ascertaining the taxpayer's income for the purpose of the Income War Tax Act . . . ." That is drawn on the basis that the person, on January 1, 1949, was the person who had already the property all through.

Mr. GAVSIE: It would only be applicable during the years he was the owner, and it would only go back to the year he acquired the asset.

Hon. Mr. HAYDEN: I know that is the intention, but I am not sure that the language is not confusing. However, so long as you say that is the intention it is all right.

The CHAIRMAN: Just before we leave this subsection, what is the significance of the words "or should have been taken into account"?

Mr. GAVSIE: You will remember the practice of the Department was to accumulate 50 per cent of the normal depreciation in the year of loss, and that was not actually taken but was accumulated for depreciation purposes.

The paragraph was agreed to.

The CHAIRMAN: The next is paragraph (*b*), which refers to the case of a taxpayer who was resident in Newfoundland on the expiration of March 31, 1949. The same formula is made applicable to him, I take it.

Mr. GAVSIE: It is a slightly different formula. It is the capital cost minus the greater of the actual reserves that he has on the books or one-half the actual depreciation that he would have taken if he had been in Canada in those years.

Hon. Mr. HAYDEN: I am trying to find the reference in (*b*) at the top of page 9, which says "one-half of all amounts allowed to the taxpayer under subparagraph (ii) of paragraph (*n*) of subsection one of section six of the said act . . ."

Mr. GAVSIE: That is the Income War Tax Act.

Paragraph (*b*) was agreed to.

The CHAIRMAN: The next is paragraph (*c*). What is that?

Mr. GAVSIE: That is what I referred to a moment ago. Special depreciations taken in 1948 or 1949 are deemed to have been taken at the beginning of 1949, so as to come under the system. Subsection (2) does away with the old Income War Tax Act recapture, because it is taken care of by this paragraph (*c*).

The paragraph was agreed to.

The CHAIRMAN: Now we pass over to page 10, subsection (2), which provides that the second and third provisoes to paragraph (*n*) of subsection one of section six of the Income War Tax Act are not applicable to sales made after the commencement of the 1949 taxation year.

Hon. Mr. VIEN: What are those provisos?

Mr. GAVSIE: Those were for the recapture of the special depreciation granted under the Income War Tax Act. Those two provisos contain a provision for going back to reassess. They are eliminated because paragraph (*c*) of section one takes care of that.

Hon. Mr. VIEN: But those provisos will not be applicable to questions arising from income taxes prior to the 1st of January 1949? All questions arising from income prior to the 1st of January 1949 will be dealt with under the law as existing then, is that correct?

Mr. GAVSIE: We go back to the case where a person got special depreciation during the war and sells the asset in 1950. If this subsection were not included the old law would be applicable to him, and on the sale the department would have to go back and look at the years in which he took special depreciation and say that because of the sale we are now going to re-write the depreciation that you took in those prior years and reduce it to normal depreciation and wipe out the special part of the depreciation that you took. That would have the effect of adding to his tax liability for those particular years in which he took special depreciation and he would get a reassessment for those previous years and have a liability for interest. That is in the Income War Tax Act. Subsection (2) says that those provisions are no longer applicable to sales made after 1949, and in lieu thereof section 8(1)(*c*) says that an extra depreciation is deemed to have been allowed at the very commencement of 1949, so that it comes into the new system.

Hon. Mr. CAMPBELL: I think Senator Vien's point was that this new arrangement will not affect any transactions of sale or otherwise prior to 1949.

Mr. GAVSIE: That is right.

Hon. Mr. VIEN: Or any other claim with respect to taxes on depreciation arising out of operations which took place prior to 1949.

Mr. GAVSIE: Except to the extent that I have been discussing. If special depreciation was taken in, say, 1947 and the asset is sold in 1950, under the old law the 1947 assessment would have been reopened. That is being wiped out, and in place of it is the provision that that special depreciation, not the normal part of it but the part above normal, is deemed to have been allowed in 1949. So the part above normal would come into play here as deemed to have been allowed in 1949, and in the event of disposal of the asset would be subject to recapture in the year of disposal rather than in the high tax years during the war.

Hon. Mr. HAYDEN: That is very beneficial.

Mr. GAVSIE: Yes.

Hon. Mr. VIEN: Is it exclusively beneficial?

Hon. Mr. HAYDEN: Yes, on a quantum basis.

Mr. GAVSIE: Unless, Colonel, the rates in subsequent years are higher than they were in the war years, it will be beneficial.

Hon. Mr. HAYDEN: It would only apply to individuals, because the corporation taxes are the same for all corporations.

Hon. Mr. MCLEAN: Back in 1942 and 1943 we were encouraged to build extensions to our plants in order to increase exports to the United States. Extra depreciation was allowed in such cases. Is that opened up again?

Mr. GAVSIE: No. That was under the War Exchange Conservation Act. We are talking about the special depreciation that was allowed by certificate of the War Contracts Depreciation Board, under the Income War Tax Act.

Subsection (2) was agreed to.

The CHAIRMAN: Now we come to subsection (3) which deals with the capital cost of property deemed lesser of actual cost. That is what the marginal note says.

Mr. GAVSIE: That has to do with a transaction not at arm's-length.

Hon. Mr. HAYDEN: What is meant by "deemed lesser of actual capital cost"?

The CHAIRMAN: In certain circumstances the capital cost to the taxpayer is deemed less than the actual cost.

Hon. Mr. HAYDEN: I understand that, but it does not mean anything to say that the capital cost of property is deemed lesser of actual capital cost. If it said "less than the actual capital cost" I could understand it.

Hon. Mr. HAYDEN: Some of these refinements are either modern or—

The CHAIRMAN: It looks like an error. We could ask Mr. Gavsie to sum up the meaning of the section in a few words, and indicate the cases it covers.

Mr. GAVSIE: There are so many of these sections I must read it to make sure I have the right one. This covers the case where a property belonging to company A has been sold to company B, a related company before 1949. You see by clause 8 the rules for determining capital costs. In that case we say the capital cost to company B, which is a related company—

Hon. Mr. EULER: You mean a subsidiary company?

Mr. GAVSIE: Yes, or a commonly controlled company. It applies only in that case, and does not apply to strangers at all—only to where they are related taxpayers, or related companies who are taxpayers. The capital costs shall be

deemed to be on the lesser of: (*a*) the actual capital cost of the property to the taxpayer (in other words, the actual amount that company B paid) or (*b*) the amount by which the capital cost of company A, the original owner, exceeds the aggregate of the normal depreciation allowed.

The CHAIRMAN: Is it not the depreciation value on the books of the vendor?

Mr. GAVSIE: Yes.

Hon. Mr. HAYDEN: Why should it not be the fair market value less depreciation? I have looked at the definition of "arm's length", and it reads as follows:

> For the purpose of this Act,
>
> (*a*) a corporation and a person or one of several persons by whom it is directly or indirectly controlled;
>
> (*b*) corporations controlled directly or indirectly by the same person; or
>
> (*c*) persons connected by blood relationship, marriage or adoption;
>
> shall, without extending the meaning of the expression "to deal with each other at arms length", be deemed not to deal with each other at arms length.

Now, surely the principle set out earlier in these amendments in relation to transactions at arms length, could very well be put on the basis of their market value.

Mr. GAVSIE: These are transactions which took place before 1949. You will remember that the rule in the first part of this was the capital cost, that is the original cost, less the depreciation taken. The application here is, if you have made a sale prior to 1949 to a related company.

Hon. Mr. MCLEAN: Would you explain what "related company" means?

Mr. GAVSIE: Transactions not at arms length; that is between those taxpayers who are not at arms length.

Hon. Mr. EULER: What does that mean?

Hon. Mr. MCLEAN: This definition reminds me of Ed Wynne's definition of why he was carrying an 11-foot pole. He said he was carrying it to touch those people that he wouldn't touch with a 10-foot pole.

Hon. Mr. CAMPBELL: Mr. Gavsie, is it not true that under the present practice, where you have a transaction or sale, or transfer of property from one taxpayer to another, not at arms length, the minister has always looked into the transaction and in most cases allowed the depreciation on what he considered to be the proper value, taking into account depreciation formerly taken? Actually that has been attempted with the legislation as it now stands. Under this section you are trying to spell out in proper language something to cover that particular type of transaction between two persons who are not, in effect, dealing in a manner so as to get taxation benefits by the transfer of a property which has been depreciated to another person or another company. That, as I understand it, is what is sought by this section.

Mr. GAVSIE: That is right.

Hon. Mr. CAMPBELL: Now, as to the language of the section, you first take the capital cost to the original owner and calculate the aggregate of the total amount of the depreciation taken for various purposes; the basis of depreciation is the amount by which that capital cost exceeds the depreciated value. Am I right?

The CHAIRMAN: By which it exceeds the depreciation.

Hon. Mr. CAMPBELL: Yes, by which it exceeds the depreciation.

Mr. GAVSIE: Yes.

Hon. Mr. CAMPBELL: It is not very clear, but I think that is what it means.

Hon. Mr. HAYDEN: What I am getting at is if a transaction took place before 949, and the vendor and purchaser were not at arms length, for the purpose of his section you are assuming the capital cost is the depreciated capital cost to he vendor. Is that right?

Mr. GAVSIE: Not less than that.

Hon. Mr. HAYDEN: My question is why should it not be taken at the fair narket value. If you are attacking the transaction, then why not put it on the air market value? The original capital cost may not be correct.

Hon. Mr. NICOL: Out of the original capital cost you take the depreciation?

Hon. Mr. HAYDEN: Yes.

Hon. Mr. NICOL: And if it were taken at the fair market value, you could ot take away the depreciation?

Hon. Mr. HAYDEN: Yes, it would be the fair value less—

Mr. GAVSIE: You might be picking up what heretofore was an untaxed roperty.

Hon. Mr. CAMPBELL: Is not the answer to Senator Hayden's question the act that there is no real change of ownership?

Mr. GAVSIE: Yes. That is right.

Hon. Mr. CAMPBELL: And you have to come back to the capital cost, less epreciation?

Hon. Mr. HAYDEN: You are dealing with a legal assumption, because they ere not at arms length. Some of these transactions might be at arms length, nd the price paid might be at a fair market value at that time.

Mr. GAVSIE: If the parties were at arms length, the section does not apply.

Hon. Mr. HAYDEN: But you are assuming, legally speaking, they weren't at rms length, according to your definition; therefore, the price paid is a fictitious rice.

Mr. GAVSIE: That is a presumption, and the rule is laid down; it is the lesser f those two items.

Hon. Mr. PATERSON: May I ask the definition of "arms length"? For nstance, are the Canadian National Railways and the Canadian National teamships at arms length?

Hon. Mr. HAYDEN: They are not at arms length, but it does not matter ecause they do not pay taxes.

Hon. Mr. PATERSON: Would the Canadian National Steamships and the anadian National Telegraphs be regarded as at arms length?

Hon. Mr. HAYDEN: No.

Hon. Mr. PATERSON: Suppose the Canadian National Steamships sold a eamer which had been depreciated by half—?

Hon. Mr. NICOL: To whom?

Hon. Mr. PATERSON: Suppose they sold it to the railway?

The CHAIRMAN: It is a wholly owned subsidiary.

Hon. Mr. PATERSON: It is a wholly owned subsidiary, but what is the situa-on there?

Hon. Mr. CAMPBELL: They could not get depreciation twice.

Hon. Mr. HAYDEN: I have no further objections.

Hon. Mr. CAMPBELL: I move the section be carried.

Section 8 (3) was agreed to.

The CHAIRMAN: We are now on subsection 4.

Hon. Mr. CAMPBELL: Carried.

The CHAIRMAN: That subsection has the same effect, I think, as the one we discussed previously.

Mr. GAVSIE: That is right.

Section 8 (4) was agreed to.

The CHAIRMAN: Subsection 5 of section 8 reads "reference in this section to depreciation shall be deemed to include a reference to allowance in respect of depreciable property of a taxpayer under paragraph (*a*) of subsection (1) of section 5 of the Income War Tax Act".

Hon. Mr. CAMPBELL: Is that the section which deals with payments made by an employer to an employee?

Hon. Mr. HAYDEN: No, we are not that far yet.

Mr. GAVSIE: That is the next section.

Hon. Mr. HAYDEN: What is the objection to that subsection?

The CHAIRMAN: Section 5(1)(*a*) of the Income War Tax Act deals with depletion and relates to income derived from mining, oil and gas wells and timber limits where an allowance is made for the exhaustion of the mines, wells and timber limits. This provides that depreciation as used in this section shall include depreciation as granted under 5(1)(*a*) of the Income War Tax Act.

Hon. Mr. HAYDEN: That means, Mr. Chairman, that when I come to ascertain the cost at January 1, 1949, that I not only deduct from the capital cost of the property the depreciation that may have been taken, but I also have to deduct the depletion allowance?

Mr. GAVSIE: Where depletion was on a cost basis. There were certain rules of depreciation where you took the cost of the property and divided the number of units of, say, a stone quarry, where you had the so-called bedded deposit. You said that that property cost you $100,000 and you were going to get X cubic feet of stone out of it. The depletion allowance was based on the units produced. You took the units to be produced, divided them into the cost of the property, and that was your depletion allowance.

Hon. Mr. HAYDEN: And you are going to deduct from the ascertainment of capital cost on January 1, 1949, the amount of any depletion that has been taken.

Mr. GAVSIE: That $100,000 may have been recovered in part by taking out the stone, and therefore we want to find out how much of that $100,000 is left to be recovered, so that the amounts that were allowed under 5(1)(*a*) would be deducted in arriving at the 1948 cost.

Hon. Mr. HAYDEN: I understand the formula, but I am questioning the policy of deducting depletion.

Dr. EATON: Under the Income War Tax Act there were certain allowances as a deduction in order to enable the taxpayer to recover his costs. One of these was depreciation, what was expended for machinery, equipment and buildings. The other was what you might call the inventory of your ore body. The allowances were granted not only under section 6 of the Income War Tax Act for depreciation but under section 5(*a*) to recover cost in respect of a wasting asset.

Hon. Mr. HAYDEN: I can understand the depreciation that related to the asset, but depreciation is the allowance you make out of what would otherwise be taxable income for the year because of the fact that by taking out that material you are exhausting the mine.

Dr. EATON: Well, they are both the amortization of the capital cost.

Hon. Mr. HAYDEN: But the depreciation is amortizing the capital cost.

Dr. EATON: The depreciation is amortizing the capital cost. In certain cases under subsection (*a*) depletion allowances were on a unit basis. That is, if you get a value placed on that ore body or bedded deposit, or whatever it is, and as it is extracted the deduction is allowed of a proportionate part of that original capital cost. It is amortizing that capital cost and amortizing it over the length of life of the property. So you have two directions in which you are recovering the capital cost.

Hon. Mr. HAYDEN: Have you had any representation from mining companies for or against this particular formula?

Dr. EATON: No.

The CHAIRMAN: Carried.

Hon. Mr. NICOL: Now I think we are through with these two sections and I suppose Mr. Gavsie will have the responsibility of carrying them out.

Mr. GAVSIE: No, the Governor in Council, senator. I just happen to be the "front man" for today.

Hon. Mr. NICOL: Can you tell me how much more you will collect under these amended two sections?

Mr. GAVSIE: I cannot tell you. We anticipate that if anything the taxpayer will get more rather than less allowance, so that presumably we will collect less. There is certainly no intention to pick up any more revenue. It is to make a simpler system.

Hon. Mr. NICOL: I withdraw my motion to throw out these sections, because of the explanations you made and the promise given by the minister.

Mr. GAVSIE: Thank you. In dealing with that part: as the questions came up I began to take with a grain of salt the statement made earlier, that the senators did not understand the section, because the questions indicated that they understood it as well as if not better than we understand it.

Hon. Mr. HAYDEN: I hope that persists.

On section 9—payments by employer to employee.

The CHAIRMAN: This is an amendment to provide for a new section of the Income Tax Act, No. 24A.

Hon. Mr. HAYDEN: This is where, for instance, a hockey player gets a bonus for signing a professional contract: the bonus would be taxable income under this amendment?

Mr. GAVSIE: That could be.

Hon. Mr. CAMPBELL: This was contained in the resolutions earlier in the year.

Mr. GAVSIE: Yes.

The section was agreed to.

On Section 10: computation of taxable income.

Hon. Mr. HAYDEN: I don't think we need spend much time on that, except to suggest that it might be increased.

The section was agreed to.

On section 11—medical expenses.

Hon. Mr. CAMPBELL: That just enables people to take it in any twelve-month period rather than the calendar year?

Mr. GAVSIE: That is correct, sir.

The CHAIRMAN: As to subsection (5), that is extending the limit to five years?

Mr. GAVSIE: Correct.

The CHAIRMAN: Subsection (7) relates to the application of the section.

Hon. Mr. HAYDEN: How do you deal with a situation prior to that time? Have you been allowing it in many cases?

Mr. GAVSIE: This is to make the law conform to the practice.

On section 12—dividends received by a corporation.

Hon. Mr. HAYDEN: This is beneficial. What do you do, for instance, if you have a foreign subsidiary, say, in England and the parent company here, and the taxes in England are higher than the corporate taxes here, so that the subsidiary in England would pay at the higher rates on these profits?

Dr. EATON: That is right. We are just saying that we will not tax that again. It is removing double taxation by just not taxing.

The CHAIRMAN: Shall section 12 (1) carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Shall section 12, subsection 2, carry?

Some Hon. SENATORS: Carried.

On Section 13—resident in Canada part of a year.

Dr. EATON: The new system is to tax an individual resident in Canada during part of the taxation year, and who is during some other part of the year not resident in Canada, on the income earned in Canada, apportion his exemptions and then determine his tax liability.

Hon. Mr. HAYDEN: That is actually the way it was done for years. I know that in relation to professional baseball players, they just tax them on the earnings in Canada. They have done that for years.

Dr. EATON: This is for a non-resident person performing services in Canada.

The CHAIRMAN: Does section 13, subsection 1 carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Does section 13, subsection 2 carry?

Some Hon. SENATORS: Carried.

On section 14—life insurance corporations.

Hon. Mr. HAYDEN: Would Mr. Gavsie explain that?

Mr. GAVSIE: The change is that we have just taken out section 28 in the Act. As we have section 28 out of the Act. we have to amend this section so as to remove the words "28".

Section 14 was agreed to.

On section 15—computation of tax.

Section 15, subsections 1, 2, 3 and 4 were agreed to.

On section 16—employee not resident during last year of employment.

Mr. GAVSIE: With respect to an employee on retirement getting a lump-sum payment, there is an option for his being taxed as a separate person rather than including it in his income for the year. This provision primarily arose because of the fact that Newfoundland came into Confederation, and the person did not have an actual previous year of taxation in Canada. So what we say is what his taxation would have been had he been in Canada.

Some Hon. SENATORS: Carried.

The CHAIRMAN: Shall section 16, subsection 1 carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Shall section 16, subsection 2 carry?

Some Hon. SENATORS: Carried.

Section 16, subsections 1 and 2 were agreed to.
Section 17 was agreed to.

On section 18—rates.

The CHAIRMAN: This section deals with corporation taxes. It provides for a 10 per cent tax on the first $10,000, and 33 per cent thereafter.

Hon. Mr. McLEAN: I should like to find out more about these related companies. I think it is very unfair that we are given a bill at 11 o'clock in the morning to study. It seems next to impossible to go over a section like this unless you spend two or three hours on it. We have found fault with the press in the Senate, but rushing things of this importance is no way in which to get a good press. I just had time to make a few notes on it, and I am going to discuss them and then get an explanation later.

With regard to Section 18, this is certainly class legislation as it discriminates against many hundreds of small companies with tens of thousands of minority stockholders many of them widows and orphans. These companies were set up in the ordinary course of business. There was no intention on their part of evading taxation in any way. Some were started to gain more economical operation—others in order to get the best management they thought available. Companies can be related to one another and be in an entirely different line of business. I can think of small utility companies set up in certain districts to help out the community, or small insurance companies.

Take along our border of the United States, a small Canadian company may be operating and related to another Canadian company, whereas right alongside of them and in competition with them, would be an American company related to a larger company or partnership across the border. Now the latter will get the benefits of the reduction in taxation, whereas the Canadian company will not. How is the Canadian company going to meet competition? Often the head of a family business may die and the heirs may be children or women and they sometimes seek an affiliation with larger companies in order to secure management. The latter company may, or may not invest in a portion of the stock of the smaller company, but generally they do. Why show suspicion of these companies, who over the years have conducted their business in a straightforward manner and especially penalize thousands and thousands of minority holders, mostly small investors. They are minority holders often through circumstances beyond their control and there is no reason to believe that in future these companies would do anything to evade taxation. There would be no objection whatever to a clause restricting large companies in future breaking up into smaller companies in order to take advantage of the Act, but to make the Act retroactive and especially penalize small companies whose setting up had nothing to do with the Act or taxation of any kind.

I can give many concrete cases where the Act would prove, as it now reads, unjust and unfair and if put through as is, it would be impossible for minority holders to help themselves. They would be unreasonably discriminated against through no fault of their own, and while their competitors get a reduction in taxes they are being denied their rights. They have gone on for years the same as other companies, looking toward the day when a reduction in taxation would come to them and now, through this class legislation, it is being held up in an absolutely unfair way. In fact their taxes are being raised 3 per cent adding insult to injury. A great majority of these companies have separate audits by professional accountants, and what profits they make have little or nothing to do with other companies which they might be related to. In any case the latter will have their own audits which the government can demand. These separate

companies might perhaps be related to an entirely different kind of business. For example, you might assist in the establishment of an electric light, heat and power company to serve your own community, and such company would not be allowed the benefit of the 10 per cent tax but would have to pay at a higher rate. If there is any explanation of that I would like to have it.

The CHAIRMAN: I think your remarks, Senator McLean, are directed against the policy rather than the mechanics of the act. As Mr. Sinclair, Parliamentary Assistant to the Minister of Finance, is here he may be the appropriate one to make some comment on your statement.

Mr. JAMES SINCLAIR (Parliamentary Assistant to the Minister of Finance): Mr. Chairman, the intention of the section is not so much to help small businesses as to help the small businessman who is in the less than $10,000 class and has only one business. If this had been applied to all small businesses a great injustice could have been worked. Take, for example, a man who is the controlling owner of four companies, each around the $10,000 profit level. Say he owns a half-interest in each. If the 10 per cent and 33 per cent rate was not applied to each company, all his profits would be taxed at 10 per cent. In other words, with an income of $20,000 from those four companies his business profit tax would be only 10 per cent, whereas his neighbour who owned only one company making the same profit would be taxed at 10 and 33 per cent. The intent here was to help the little businessman, the owner of one small business, who finds the old 30 per cent rate too heavy. In the debate in the House of Commons points such as Senator McLean has made were raised, and Mr. Abbott said that while the intent was to help those individuals who probably constitute 90 per cent of the small business owners, there was no desire to inflict an injustice on minority holders in other companies. He pointed out that the effect of this would not actually be reflected in tax returns until next year, and as this is an entirely new principle so far as corporation taxation is concerned he would like to make a further review of it over the next three or four months—not a review of the principle, because the government thinks this is a good principle, but a review of the situation such as Senator McLean has described.

Hon. Mr. MCLEAN: Look at the position of any Canadian company which is trying to compete with an American company that has a subsidiary in Canada. We do not know who the partners of the American subsidiary are, but the company will get off with a 10 per cent tax. Our companies cannot possibly compete under these conditions.

Dr. EATON: But when the American company's profits are moved to the United States, they will be taxed 38 per cent, as compared with the Canadian company's tax of 33 per cent.

Hon. Mr. MCLEAN: But the American companies are allowed to write off any taxes they pay in Canada, and we lose the difference.

Dr. EATON: The Canadian treasury loses the difference.

Hon. Mr. MCLEAN: And the American tax rate might be cut to 25 per cent next year, so far as we know.

Dr. EATON: I am only pointing out the present situation.

Hon. Mr. MCLEAN: I can point to cases where cold-storage companies have been organized for the benefit of a local community, and the cold-storage business is entirely different from that of the parent company. And I know of cases where light, heat and power companies have been organized and carry on entirely apart from the parent company's line of business. The object in these cases is more or less philanthropic, to help the local community. Then take the case of a family corporation which, when the main partner dies, seeks

the aid of a larger corporation for management purposes. The product of the small company might be entirely different from that of the parent company. Such transactions as that are viewed with suspicion under this bill.

The CHAIRMAN: Are you thinking of the case where the minority shareholders of the subsidiary companies would be different in each company?

Hon. Mr. McLEAN: Yes, I could name dozens of companies of that kind who would be penalized. Perhaps 50 per cent of the minority shareholders are not in the management at all; they sought management outside, and there was no objection whatever to that when the companies were set up. If you want to prevent that kind of thing from being done in future, all right, but I say that this should not be applied to the companies that are already set up. I think it is extremely unfair and that some amendment should be made. And I would point out, Mr. Chairman, that this is our last opportunity for dealing with it.

Hon. Mr. CAMPBELL: Mr. Chairman, I would like to refer to subsection (4), which says:

> For the purpose of this section, one corporation shall be deemed to be related to another in a taxation year if, at any time in the year,
> (*a*) it, directly or indirectly, controls the other,
> (*b*) it is, directly or indirectly, controlled by the other, or
> (*c*) both corporations are controlled, directly or indirectly, by the same person.

Senator McLean has made quite a good point here, but we must bear in mind that prior to the introduction of this legislation all the companies to which he refers were subject to the higher rate of tax. In other words, they were still related companies and were paying at 33 per cent. This reduction in tax to 10 per cent on the first $10,000 is a relieving provision, and there must be some control such as is contained in this bill, because in the complexity of industrial life there are a great many subsidiary companies. For instance, a steamship company might be operating 30 boats, each in a separate company, and without some control such as this each of these companies might pay only 10 per cent on its first $10,000 of earnings, whereas another company having all its boats under its own name, would be taxed at the higher rate. That would be a discrimination in favour of the operator who had a number of companies. The explanation has been made that the purpose of the legislation is to benefit the small businessman and not the person who controls many companies. True enough, it is a bit of a hardship on the minority shareholders, but it is very difficult to provide for all cases.

Hon. Mr. McLEAN: In answer to Senator Campbell, may I say, your steamship companies have set up separate companies so that the liability will not be so great; you have got full benefit all these years, and you will have it in future years. They have set up those companies with their eyes wide open. The companies to which I refer set themselves up without knowing anything about this Act; they have not done so to limit their liability. That is self-evident.

Hon. Mr. CAMPBELL: The steamship companies did not set themselves up to escape taxation.

Hon. Mr. McLEAN: They had a purpose in doing it but that is not so with the small companies I am talking about.

Hon. Mr. DUPUIS: May I say a word, Mr. Chairman, although I am not a member of the committee?

The CHAIRMAN: Certainly.

Hon. Mr. DUPUIS: I have in mind a parent company of one of my clients who is very strongly against the imposition of such taxes. I have received a wire in which the president of the company says in part as follows:

> A parent company's subsidiary and affiliated company earnings would be taxed thirty-three per cent instead of each subsidiary company being allowed the seventeen per cent rate on the first ten thousand dollars of earnings the same as permitted all other companies. Might we suggest the new resolution apply only to such subsidiary and affiliated companies as are formed after the date of the introduction of the new resolution.

I wrote to the Minister of Finance, and he replied, acknowledging receipt of my letter and in the second paragraph said these words:

> I expect that the question of related companies will be fully discussed in the House when Bill 176 comes up for second reading and I shall be glad to give careful consideration to Mr. Prescott's suggestion that the amendment dealing with related companies should apply only to subsidiary and affiliated companies formed after the date of the introduction of the amending Bill.

In this case the parent company is making artificial leather, and one of the subsidiary companies is making a fertilizer for the use of farmers out of the residue of the product of the parent company. The subsidiary company is of interest to the farmers and businessmen in the surrounding area, who have taken shares in the company. They are not at all interested in the parent company. With this new legislation they would be penalized because the company is a subsidiary. I do not know what was done in the other place, but I think it most unfair that subsidiary companies which are now in existence should be penalized. I would beg leave of this committee to make a suggested amendment, that this legislation become effective for subsidiary companies only after the passing of the bill.

In the last paragraph of Mr. Prescott's letter, he said:

> You will recall that during wartime when the question of Excess Profit Taxes arose, tax regulations were put into force preventing parent companies from forming subsidiary companies and thus obtaining tax benefits, but all the wartime measures did not presume to penalize subsidiaries established prior to the introduction of the specific Excess Profit Tax regulation. It was then a recognized fact—when indeed the Government needed and did take every bit of taxation possible—that it was unwise and unfair to penalize previously established subsidiaries. Why then should the present tax resolution reverse the established practice of the past?

The CHAIRMAN: I think the problem, senator, is that the remedy might be probably worse than the disease.

Hon. Mr. DUPUIS: I do not know.

The CHAIRMAN: You would have one tax applicable to companies formed before a certain date, and another rate applicable to companies formed after that date. That is a form of discrimination.

Hon. Mr. DUPUIS: Yes, but we have many precedents of certain tax legislation which applies only after the passing of the Act, and which is not retroactive. Why should this one be retroactive?

The CHAIRMAN: This provision is not retroactive.

Hon. Mr. DUPUIS: It penalizes the already established subsidiary companies.

Hon. Mr. MCLEAN: Mr. Chairman, the Minister or the department must be satisfied in this respect. It is easy to get evidence of new subsidiaries set up after this Act to avoid taxation, but if they cannot satisfy the Minister on the

point there is no objection to putting in a restriction or a guarding clause. These companies of which I speak were set up and had nothing to do with taxation whatsoever, but they are now caught.

Mr. SINCLAIR (M.P.): But businessmen for exactly the same reason—

Hon. Mr. McLEAN: But I do not like the idea of being suspicious of everybody. If subsidiaries formed for the purpose of getting off easier in taxation cannot satisfy the department, then the department would not have to allow them anything. As to these companies of which I speak, we can go back and satisfy anybody in the department from the evidence that the companies were not set up to evade taxation in any shape or form. If companies in the future cannot satisfy the department, there is no reason why they should not be taxed.

Hon. Mr. McDONALD: Mr. Chairman, what amount of revenue is expected from the application of this section?

Hon. Mr. HAYDEN: None. That is what we were told this morning.

The CHAIRMAN: As I understood the statement it was the reduction by virtue of 10 per cent on the first $10,000 would be set off by the income from the additional 3 per cent, with the result that the total amount of corporation taxation would be about the same; in other words, the burden on the shareholder in the aggregate will not be changed.

Hon. Mr. CAMPBELL: Mr. Chairman, I have every sympathy with the small shareholder in the minority group, provided he owns just a few shares in his company. But if we give effect to the argument presented here by Senator McLean, and others, that the greatest benefit is in favour of the controlling interest—in other words, if we extend this principle to include all companies related or otherwise, prior to 1949, then the person who gets the greatest benefit is the large shareholder who has control of many companies.

The CHAIRMAN: Right.

Hon. Mr. CAMPBELL: I do not think that is intended by the legislation. As this is a relieving section, new in principle, I think it is a favourable provision meant to help out the small businessman. We should, therefore, adopt the section as it stands, and I so move.

Hon. Mr. McLEAN: In reply to Senator Campbell, I would ask him how is it going to help the one who is managing the company? The books of most of these companies are audited by a chartered accountant; they have their own profits. Take for instance a utility company operating in a small town, and for economic reasons the town manages the company; the books are all under the public utilities board, and their profits are audited and a statement submitted. In those circumstances, how on earth is this section going to help out the parent company? It is ridiculous to say that it would.

Hon. Mr. CAMPBELL: I think the explanation is very simple. For instance, assuming you control ten companies earning $10,000 a year; that means there is $100,000 annual earnings from those companies. You get your share of 50 per cent of those earnings, which is $50,000, subject to 10 per cent. Now, the minority shareholders in these other companies will undoubtedly be spread over many people, and in effect, you as a large shareholder in these ten companies will benefit greatly, as against the other man who has one company earning $100,000.

Hon. Mr. McLEAN: Well in a parent company generally $10,000 would not amount to such an awul lot. There are very few companies where you would find ten or more getting any advantage from this taxation, but I certainly know a lot of companies where the larger company has helped out by practical philanthropy, smaller companies to give a public service. It may be cold storage, it may be light, heat and power service or something like that, but something that is entirely unrelated to the product or manufacture. A company in the mining or the lumber business may go into something to help the

community, the town or county. It seems to me that this would penalize such activities. It does not mean an awful lot to the parent company, but it means a lot to companies doing a public service.

Hon. Mr. CAMPBELL: I can suggest a method by which it could easily be overcome—by the controlling interest selling a few shares, so that it holds something less than a majority.

The CHAIRMAN: So that it would be no longer a related company.

Hon. Mr. CAMPBELL: It would be no longer a related company.

Hon. Mr. HUGESSEN: Although the amendment suggested by Senators McLean and Dupuis might be helpful to the particular small companies to which they refer, the real benefit of any such amendment would accrue to large corporations with a large number of subsidiaries. Take the Canadian Pacific Railway: probably there are fifty or sixty operating subsidiaries, and the benefit to them would be, instead of having one $10,000 free of income tax, they could have fifty or sixty paying only the 10 per cent. That would be the real benefit of that amendment.

Hon. Mr. DUPUIS: I would like to suggest this while I am on the subject, following the argument of Senator Hugessen that this would create an injustice to the taxpayer of this country because a large company like the Canadian Pacific Railway would have too much benefit through its subsidiaries. May I suggest that section 36, subsection (1), paragraph (*a*) should read: "10 per cent of the amount taxable if the amount taxable does not exceed $30,000." Then you could have a small subsidiary.

Hon. Mr. NICOL: That would make it worse.

Hon. Mr. DUPUIS: I don't think it would.

Hon. Mr. NICOL: We would all have subsidiaries then.

Hon. Mr. DUPUIS: That is right. I am wrong.

The CHAIRMAN: I am afraid that would aggravate the problem.

Hon. Mr. DUPUIS: Yes, I quite agree. But my idea is to have the small subsidiaries.

The CHAIRMAN: I think everybody appreciates the point, and we have been assured that the minister is going to review the matter over the next three or four months, so perhaps we might be content with that and take the question on the section now.

Hon. Mr. LAMBERT: That was the point I wanted to make, and which Mr. Sinclair made.

Hon. Mr. DUPUIS: If the minister is going to review this three or four months ahead, that creates an injustice to these small subsidiaries. Anyway, my idea is to move an amendment to subsection (1) of section 36, paragraph (*a*).

The CHAIRMAN: I am afraid you are in this position, senator: you can speak, but not being a member of the committee you cannot vote.

Hon. Mr. DUPUIS: Oh, no, I am not a member of the committee.

The CHAIRMAN: You have made your suggestion.

Hon. Mr. McLEAN: I will move the amendment.

The CHAIRMAN: Whatever it is!

Hon. Mr. McLEAN: It is applying to all companies. That is what you mean?

Hon. Mr. DUPUIS: Yes.

Hon. Mr. McLEAN: I move an amendment that it shall apply to all companies, that the word "related" be taken out, and that it apply to any company, subsidiary or otherwise. The amendment can be moved and the appropriate words put in afterwards.

Hon. Mr. CAMPBELL: I do not think there is anyone to second the motion.

The CHAIRMAN: That is unnecessary. Perhaps, Senator McLean, we can deal first with subsection (1), to which your amendment does not relate. Shall subsection (1) be adopted?

Carried.

Now we come to subsection (2), "related corporations." That, I think, is the one to which Senator McLean's remarks are directed. It says:

> Where two or more corporations are related to each other in a taxation year, the tax payable by each of them under this part for the year is, except where otherwise provided by another section, 33 per cent of the amount taxable for the taxation year.

And subsection (3) provides:

> Notwithstanding subsection (2), where two or more corporations are related to each other, the tax payable by such one of them as may be agreed by them, or if they cannot agree, as may be designated by the minister shall be computed under subsection (1).

Hon. Mr. DUPUIS: May I know from the Parliamentary Secretary of the Minister what happened about this request of Bennett Limited about this section 36?

Mr. SINCLAIR: Senator, that was but one of many letters that we received, and it was because of that that the minister gave his assurance in the house. He said that the present subsection covers at least 95 per cent of the small businesses which it was the intent to help. It also stops the abuse of this section by big companies who wanted a split-up, and he gave the house the assurance which was in that letter, that for that little group of related companies for which it is very difficult to make provision and yet be fair to big companies, he would give further study between now and when the budget is brought down in March. But he pointed out that no injustice is being done to anybody at the moment, since these tax laws will not actually be effective until the returns come in next year. So if a change were made in March which would help these related companies it would be effective on this taxation year. That is why he asked that this be passed now, to give immediate encouragement to small business; but if Senator McLean and others feel that a provision could be drafted which would be fairer to these companies, and would bring it forth in the three or four months before the budget comes down, he gave an undertaking in the other house, and I know the same holds good here, to give very careful consideration to it.

The CHAIRMAN: You have heard the explanation of Mr. Sinclair. We have an amendment of Senator McLean which is not in any form, but we know the purpose and intent of the amendment. In effect it would be to strike out subsections (2), (3), (4), and (5) of section 36 as re-enacted.

Are you ready for the question? Shall the amendment carry? . . . The amendment is lost.

The CHAIRMAN: Shall subsection 2 carry?

Some Hon. SENATORS: Carried.

Section 18, subsections 3, 4 and 5 were agreed to.

On Section 19—foreign tax deduction.

Dr. EATON: That amendment is consequential upon the amendment which I referred to a while ago about the person taking up residence in Canada or giving up residence in Canada. The purpose of this subsection 1 is to prevent a person coming to Canada and being resident part of the year, from taking a tax credit in respect to income which we do not tax. That is, he has paid foreign tax to another government in respect to income that he earned while he was

absent from Canada, and we had to prevent him from taking a tax credit in respect of income which we had not taxed.

The CHAIRMAN: Shall section 19, subsection 1, carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Next we come to section 19, subsection 2.

Dr. EATON: This is the provision dealing with taxation of life insurance corporations in respect to taxes paid to a foreign government. It was never intended in principle that they should be deprived of the tax credit they previously enjoyed.

The CHAIRMAN: Shall this subsection carry?

Some Hon. SENATORS: Carried.

Section 19, subsections 3, 4 and 5 were agreed to.

On section 20—trusts or estates.

The CHAIRMAN: This section is an amendment of section 40 of the Income Tax Act by inserting a new paragraph. This paragraph provides that an estate or trust must file a return of income within 90 days of the end of its taxation year where previously the requirement was that it file on or before April 30.

Section 20, subsections 1 and 2 were agreed to.

On section 21—payment of remainder.

The CHAIRMAN: This subsection clarifies the requirement in the present subsection 2, with regard to quarterly instalment payments.

Mr. GAVSIE: There is a provision that if remuneration from which amounts have been deducted or withheld, which a person received in the year, is equal to or greater than 75 per cent of his income for the year, he does not have to make instalment payments. The question came up as to whether that 75 per cent was before the deduction was made or after it was made, and now we are making it clear that it is gross and not the net.

The CHAIRMAN: Shall subsection 1 carry?

Some Hon. SENATORS: Carried.

Section 21, subsection 2 was agreed to.

On section 22—special case.

Dr. EATON: This is the relieving section for the small co-operatives.

Hon. Mr. HAYDEN: Did they ask for this?

Dr. EATON: Not in this exact form.

Hon. Mr. MCDONALD: Is this what they asked for?

Dr. EATON: It is more than they asked for. It is consequential of the fact that they only have to pay 10 per cent on the first $10,000. It used to be that they need not make instalment payments if their income was $3,000. We have changed the word "$3,000" of income to $1,000 of tax, which in effect gives them freedom from instalment payments if their income is up to $10,000.

Hon. Mr. NICOL: At the present time co-operatives have an exemption of taxation, have they not?

Dr. EATON: For the first three years of their existence they are exempted entirely.

Section 22, subsections 1 and 2 were agreed to.

On section 23—certificate before distribution.

Mr. GAVSIE: This conforms with the new Bankruptcy Act.

Section 23, subsections 1 and 2 were agreed to.

The CHAIRMAN: Shall subsection (1) of section 24 carry?

Hon. Mr. HAYDEN: Is this after assessment?

Mr. GAVSIE: It is the same rate before and after now.

Hon. Mr. PATERSON: Is there any section there to reimburse the taxpayer or overpayment?

Mr. GAVSIE: There is a section in the Act.

Hon. Mr. NICOL: A company in which I am interested overpaid $5,000. The epartment held it for three or four years and then refunded the money without cent of interest.

Subsection 1 was agreed to.

Subsections (2), (3), (4), and (5) were agreed to.

The CHAIRMAN: Subsection 6 provides a penalty for payment in arrears.

Mr. GAVSIE: This is a relieving section. It is going to be simpler from an dministrative point of view and will help both the taxpayer and ourselves.

The subsection was agreed to.

On section 25—delay in making returns.

Mr. GAVSIE: Heretofore there was a minimum penalty of $5. We are now uggesting that it be 5 per cent of the tax, so that instead of a taxpayer having o pay a tax of $1 plus a $5 penalty, he will have to pay in all $1.05. It was bviously ridiculous where the tax was only $2 or $3 and the minimum penalty or late filing was $5.

The section was agreed to.

On section 26—municipal or provincial corporations.

Dr. EATON: In the past a corporation that was 90 per cent owned by a unicipality or province was exempt from income tax, but there was no provis- n with respect to a wholly owned subsidiary of such a corporation.

Hon. Mr. MCLEAN: Is there any provision with respect to a subsidiary that wholly owned in England, for instance? What is the withholding tax on ividends from Canada?

Dr. EATON: Parent subsidiary U.K., no tax parent U.K., subsidiary Canada, holly owned, no tax, by convention.

Hon. Mr. HAYDEN: Parent Canada, subsidiary U.S., 5 per cent?

Dr. EATON: Yes.

The section was agreed to.

Section 27 was agreed to.

On section 28—rights or things transferred to beneficiaries.

Hon. Mr. CAMPBELL: That provides that the income may be divided between ne deceased and the estate in any taxation year, does it?

The CHAIRMAN: The explanatory note says:

"Section 59 of the act deals with the income of deceased persons during the ear in which they die. Subsection (3) is new and provides that certain income ems may be taxed in the hands of the beneficiary in certain cases. Subsection 4) is new and makes special provision for the case where the deceased was not esident in Canada in all of the four years preceding his death, as for example n the case of a resident of Newfoundland".

Dr. EATON: Subsection 1 provides that rights or things that would be income re, if transferred to the beneficiary, taxable income in the hands of the bene- ciary when he receives the amount. That is a relieving section from the law t present. Subsection (4) provides for the carrying out of an option. The state of the deceased taxpayer has certain options with respect to the taxation n those rights or things that are income. This makes provision for cases where

the deceased became a resident of Canada only in the year in which he died, by providing what his taxation would have been if he had resided in Canada in the preceding year.

The section was agreed to.

Section 28 was agreed to.

On section 29—"Upkeep, etc."

Mr. GAVSIE: This is a beneficial amendment to provide that the beneficiary shall not be deemed to have received taxable income by way of use of property, unless the cost of maintaining the property was paid out of income from the estate. Heretofore, a beneficiary was taxed on the value of the premises, even though the cost of upkeep was paid out of capital.

Section 29 was agreed to.

On section 30—"Dividends declared."

Hon. Mr. HAYDEN: We now come to section 30, which is quite puzzling to figure out. The Minister has given an undertaking that there were no changes in relation to personal corporations. Somehow or other a provision got in which appears in some circumstances to tax capital. I am wondering if this is not a limited correction. It limits it absolutely to the cases of personal corporations.

Dr. EATON: No.

Hon. Mr. HAYDEN: Otherwise you have a formula to apply.

Dr. EATON: Yes.

Hon. Mr. HAYDEN: I do not know how the formula works, but supposing a corporation is a personal corporation for years and then by reason of change of residence to a foreign country it becomes an N.R.O. company for a number of years, and later returns to Canada. It would again become a personal corporation in those circumstances. If the surpluses accumulated during the period it was an N.R.O. Company were taken out, there would be no tax, but if they were left in there might be a personal tax under the formula you provide. I do not think that is the intention.

Mr. GAVSIE: All I can say is that the people who worked on this proposed legislation endeavoured to meet the things that were left out at the last session. I can assure you we will be back here for further amendments if this bill does not accomplish what we have attempted. There is a lot of language in it.

Hon. Mr. HAYDEN: I will say there is a lot of language.

Mr. GAVSIE: And I do not propose to be able to explain it.

Hon. Mr. CAMPBELL: In addition to the point Senator Hayden raises, you have now provided a ten per cent cut with respect to earnings.

Mr. GAVSIE: Right.

Hon. Mr. McLEAN: Mr. Chairman, we are going through the sections so fast we do not get a chance to read them. I may be dense, but there are things here that I do not understand. We got this bill at 11 o'clock this morning, and to shove it through this way is dangerous.

The CHAIRMAN: I am entirely in your hands.

Hon. Mr. McLEAN: We should take time to read this bill. I am not going to pass on this sort of legislation, the way it is being put through.

Hon. Mr. CAMPBELL: There is not very much in the way of drastic changes; it is more a tidying up of some of the provisions in the old Act.

Hon. Mr. HAYDEN: There is no doubt that this section 30 of the bill is beneficial to the extent that it goes. It implements a statement that the Minister made when the original act was before the committee to the effect that there

were no changes other than changes in definition. As I understand the representatives here, if the bill falls short of accomplishing its purpose, they will be back here to supplement the amendments in the bill this year. Is that correct?

Mr. GAVSIE: Yes.

Hon. Mr. HUGESSEN: May I ask this question? Has there been any change in this section since the bill was introduced in the House of Commons on November 10?

Mr. GAVSIE: No.

Hon. Mr. HUGESSEN: It is hardly fair to say that we only received the bill this morning at 11 o'clock.

Hon. Mr. HAYDEN: I have had it since then.

Hon. Mr. PATERSON: What change is made by section 30?

Dr. EATON: So far as I know it is the same as it was under the Income War Tax Act.

Just for your information, I know one chartered accountant who was concerned with the provisions of the bill. He raised some questions with the department, and they were able to establish to his satisfaction that this amendment would carry out the undertaking to restore it to its 1948 status. It took three or four exchanges of wires to do so, but it was done to his satisfaction.

Hon. Mr. HAYDEN: You mean the 1948 status?

Dr. EATON: Yes, I mean the 1948 status.

Hon. Mr. NICOL: I do not suppose the government is intending to give the powers of taxation back to the provinces.

Some Hon. SENATORS: Oh, oh.

The CHAIRMAN: This next subsection is very lengthy, but you have heard the explanation of the purpose for which it was inserted, and you have the assurance that if the remedy is not accomplished at this session by this amendment it will be remedied at a later session.

Hon. Mr. HAYDEN: Carried.

Hon. Mr. HUGESSEN: Carried.

The CHAIRMAN: Are there any further questions on it?

Hon. Mr. McLEAN: We are passing the section pretty fast. Dr. Eaton has just said that he has had the opportunity of consulting chartered accountants. I should like to consult a chartered accountant on the scope of this measure; we are not specialists on this subject.

Hon. Mr. LAMBERT: We will have to do it between now and the beginning of the next session.

Hon. Mr. McLEAN: Some sections are much more complicated than others.

Hon. Mr. PATERSON: Mr. Sinclair should bring in a bill to abolish taxation. There are 13,000,000 people in Canada trying to get out of paying taxes.

The CHAIRMAN: Not that many.

Hon. Mr. HAYDEN: I move that section 30 be carried.

Section 30 was agreed to.

On section 31—"Investment companies".

Dr. EATON: Section 31 deals with investment companies which, if they came within a certain definition, were exempted entirely from corporation taxes in the past. We introduced the provision for giving shareholders a tax credit in respect of dividends received from a tax-paying corporation. If the corporations were not tax-paying corporations, the shareholders accordingly would get no tax credit.

This amendment allows them to elect, even though the corporation may come within the definition, to be a taxable corporation, to pay taxes. The result will be that shareholders will get a tax credit—

Hon. Mr. HUGESSEN: In respect of dividends they receive from the company?

Dr. EATON: Yes.

Hon. Mr. LAMBERT: Does it come under the 10 per cent provision?

Dr. EATON: Yes.

Section 31 was agreed to.

On section 32—"Non-resident-owned investment corporation".

Dr. EATON: Subsection 1 deals with N.R.O. Companies, that is, non-resident-owned investment corporations. In the past a company was disqualified if it made loans or carried on an active business in Canada. The law said that investment companies were actually carrying on business if they made small loans. The criterion was, small loans up to $500. The result was that companies could split up into two parts, one making loans up to $500 and the other picking it up from $500. In that way they could qualify, and pay 15 per cent instead of 33 per cent.

Hon. Mr. HAYDEN: The company could still qualify as an N.R.O. Company and have loans outstanding, but it could not have the principal business of making loans.

Dr. EATON: Yes, sir.

Hon. Mr. HAYDEN: As to subsection 3, I am not so much concerned about the substance of it, but I am about the method that is being employed, namely, the declaration in relation to the Income War Tax Act. I take it that in the department there has been a practice under the Income War Tax Act to enforce a certain course of action in respect of the subject matter of subsection 3. Now you are a little concerned about whether you had the legal authority to do it. What you are saying and declaring is that it was always the law.

Hon. Mr. CAMPBELL: Does this not arise as a result of a sort of slip-up in the drafting of the section in the last act?

Dr. EATON: Yes.

Hon. Mr. CAMPBELL: I don't know how it arose.

Dr. EATON: I can tell you how it arose. In 1946 the budget resolution stated the principles under which the tax arrangement with respect to non-resident corporations would be re-organized and simplified. Under the old system a non-resident corporation which paid a tax of 22½ per cent was allowed a credit of one-third in respect of Canadian dividends and one-third of the foreign tax paid by it. The end result of these two provisions gave in most cases an effective tax of 15 per cent. The proposed revision was to establish the rate at 15 per cent and withdraw the other credit provisions, and that was clearly stated in the budget resolution. But the draftsman came along and incorporated the provision for withdrawing the one-third tax credit but omitted altogether in section 4 (*n*) to withdraw the credit to one corporation receiving dividends from another; he forgot to amend it to disallow the N.R.O. from getting the credit. The new provision was acceptable generally, lower rate with no credit, but there was a technical omission in another provision in the law which they subsequently raised and said, "How about this provision?"

Hon. Mr. HAYDEN: I can understand coming in here and wanting to correct a mistake or omission. But this refers to the Income War Tax Act.

Dr. EATON: Entirely.

Hon. Mr. HAYDEN: And to come in here some years afterwards and say "We do not want the law to be what the statute says the law was, because that was a technical omission—"

Hon. Mr. HUGESSEN: Well, Mr. Chairman, in point of fact none of these companies ever did get this, did they?

Mr. GAVSIE: There is a very grave doubt to to whether the law does allow it. The department never allowed it. I don't think the law does allow it. There seems to be some contradiction as between two sections. This is a declaration as to what was intended. It is not clear either way.

Hon. Mr. HAYDEN: Surely that is for a court. I can understand you tightening something up from the beginning of the taxation period in which you pass an act, but to go back of that, where rights have been stated by statute, and to attempt by declaration of Parliament to say what the interpretation is, instead of letting the courts do it, is just the sort of thing we have been doing under other legislation, and we have got to draw the line somewhere. I think it is a dangerous practice to get into, to attempt to declare by Parliament what was intended and what the law is in regard to a statute that was enacted several years before. I have not any concern about the particular application; I am concerned about the principle of making declarations afterwards as to what the law was in an earlier period. That is what we have got the courts for. We could do away with courts and just have judicial decisions by statute of Parliament.

The CHAIRMAN: If there is a doubt as to something in the existing legislation would it not be proper to remove it?

Hon. Mr. HAYDEN: My friend says that innocently. He says there is a doubt. The department may say there is a doubt, but the taxpayer may say there is no doubt. That usually leads to a hearing in the court, in which the taxpayer is one party and the department is the other. Why should we come to the assistance of one party or the other?

Hon. Mr. NICOL: There are no cases pending?

Mr. GAVSIE: After this legislation was drafted, some time in. I think it was, the second week in November, there was a notice of objection filed against an assessment made by the department that did not allow this. The department has consistently refused to allow it. In that sense, if you mean that sort of litigation, yes, there is one case.

Hon. Mr. NICOL: And this legislation will settle that case?

Mr. GAVSIE: No. This legislation was drafted long before.

Hon. Mr. HAYDEN: But the effect of this legislation if it is passed will be to take away whatever right a person may have. He cannot even go to the courts.

Mr. GAVSIE: This will clear up what was in the resolution very clearly.

Hon. Mr. HAYDEN: It is the principle I am concerned about.

Mr. GAVSIE: I was not here, so I am going to sit out of the argument.

Hon. Mr. CAMPBELL: I agree entirely with Senator Hayden on trying to make a declaration which is retroactive to cure faulty language in a previous act, but in this case I think it was perfectly obvious what was originally intended when the other act was brought down. No one could have any doubt about it whatever.

Hon. Mr. HAYDEN: There is one taxpayer who has served a notice of objection. . . .

Hon. Mr. CAMPBELL: I move that this section be passed.

Hon. Mr. HAYDEN: I will second it, then.

The section was agreed to.

Hon. Mr. NICOL: How many corporations of the sort we are discussing this afternoon are there?

Hon. Mr. HAYDEN: Which are affected by this?

Hon. Mr. NICOL: Yes.

Hon. Mr. HAYDEN: There may be a considerable number.

Dr. EATON: But a very limited number would be affected by this, because this is mainly on Canadian dividends. A great number of companies have foreign investments and would not be affected by this at all.

On section 33—scientific research.

The CHAIRMAN: Section 33 deals with deductions from income in respect of scientific research related to the business of and directly undertaken by and on behalf of the taxpayer.

Hon. Mr. HAYDEN: That ties in your whole appreciation plan?

Dr. EATON: That is correct.

Hon. Mr. HAYDEN: I do not want to anticipate any person else who wants an explanation: it is necessary—

Dr. EATON: To bring them under the ordinary scheme of depreciation. They had a separate depreciation set-up under a special provision of the law, and it is to ensure that the depreciation, although allowed by a separate section of the law, shall come under the ordinary regime and regulations affecting depreciation.

Hon. Mr. HAYDEN: If I contributed money for scientific research which was to be applied for the construction of a building or laboratory in which the experiments were going to be conducted, then the depreciation would apply in accordance with sections 7 and 8 of the bill in relation to that, and all the incidents will follow.

The section was agreed to.

On section 34—mining companies.

The CHAIRMAN: Section 34 deals with the taxation of mining companies.

Dr. EATON: It extends for three more years the three-year exemption for new mines coming into production.

The section was agreed to.

On motion of Senator McLean the committee adjourned to meet again at 8 o'clock p.m.

(At 8 o'clock the meeting was resumed).

The CHAIRMAN: Gentlemen, may we come to order. We are now at the stage where we are dealing with section 35 which is on page 29.

On Section 35—deduction of consolidated loss.

Hon. Mr. HAYDEN: Would somebody explain what that is about?

Dr. EATON: This amendment is consequential on the change of the carry forward from three years to five years. The underlined words there are "five taxation years" where previously it was three taxation years.

The CHAIRMAN: Does section 35, subsection 1 carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: The next is section 35, subsection 2, which deals with consolidated losses in any year.

Dr. EATON: The change there was to insert the word "taxable" in front of the word "incomes". There is a consolidation of taxable incomes.

Hon. Mr. HORNER: The farmers may understand this part but do the lawyers understand it? I do not want the lawyers to be unduly taxed.

Mr. GAVSIE: Senator Horner, sometimes it is rather hard to understand what the lawyers understand.

Hon. Mr. HORNER: I do not want to see them in any trouble.

Hon. Mr. HAYDEN: We will come to you if we are in any trouble.

Hon. Mr. HORNER: I would not like to see my good friend from Margaree orks (Hon. Mr. MacLennan) placed under any undue burden.

The CHAIRMAN: If any lawyers do not understand section 35, subsection 2, t them speak up now.

Some Hon. SENATORS: Oh, oh.

Section 35, subsection 2 was agreed to.

The CHAIRMAN: We come now to section 35, subsection 3.

Dr. EATON: This is purely a technical change. It used to be that the tax ayable was an amount equal to 32 per cent of the consolidated taxable income or the year, but instead of specifying the total rate it is provided that an dditional 2 per cent be added.

Mr. GAVSIE: Yes, and the parent company is the one that is taxed in the ase of a consolidation.

Hon. Mr. HAYDEN: Then the subsidiary would not get it?

Mr. GAVSIE: As I understand consolidations, you get the taxable incomes of l the entities and that is all taxed in the hands of the parent. Therefore, ne parent is the only taxable corporation of the group.

The CHAIRMAN: Shall section 35, subsection 3 carry?

Some Hon. SENATORS: Carried.

Section 35, subsection 4 was agreed to.

On section 36—reply to appeals.

The CHAIRMAN: This deals with the procedure in respect of appeals to ne Exchequer Court.

Mr. GAVSIE: Heretofore the section provided that the pleadings to be etermined as ordered by the court and the president of the Exchequer Court as suggested that the provision be put in the Act itself. The respondent has file in the court a reply to the notice of appeal, admitting or denying the act alleged. It is just having the proceedings provided for in the Act itself ather than having the court make an order.

Hon. Mr. HAYDEN: Where is that?

Mr. GAVSIE: It starts "the respondent shall, within 60 days from the day the otice of appeal is received, or within such further time as the court or a judge hereof may either before or after the expiration of that time allow, serve on the ppellant and file in the court a reply . . . "

Hon. Mr. GOUIN: You have changed first of all the word "may" and replaced by the word "shall", and then you have added the provision concerning the rther time to be granted by the court.

Hon. Mr. HAYDEN: All I am concerned about here is whether we are getting to a position that, if the pleadings are not technically correct, the person is oing to lose the right he has when he makes the appeal.

The CHAIRMAN: No. It just gives him the right to go to the court and the udge and amend his notice of appeal. This was not specifically provided for eretofore.

Sections 36 and 37 were agreed to.

On section 38—dividends.

Dr. EATON: This section deals with the position of non-resident owned vestment corporation. As I said a while ago, they have a special rate of tax a their income of 15 per cent. We have a provision corresponding, that their vidends may go out tax free. However, they may enjoy that tax free dividend rivilege only if they have conformed to certain conditions. One of these condi-

tions is that they pay an accumulated income, equivalent to the 15 per cent rate. After that has been done, the dividends go out tax free. There was a technical defect in the law as we wrote it for the Income Tax Bill, whereby it was extremely difficult to qualify for that privilege. This is to correct a purely technical difficulty. Another correction is that when we said that a tax had to be paid on income equal to the 15 per cent, all we were aiming at was that they should have paid a tax on distributable surplus. Income as defined, was income as defined on the law on which the tax has been paid. There was no fund there to distribute the whole of the income, and so the law has been amended to strike out the word "income" and to use the word "surplus" as defined by the regulations. Those are the two technical changes.

Hon. Mr. HUGESSEN: I think that is an improvement.

Dr. EATON: Yes.

The CHAIRMAN: Does subsection 1 carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Subsection 2 deals with rents and royalties, etc.

Mr. GAVSIE: What has happened is that in the non-resident provision we are revoking the provision for withholding tax on copyrights, and what will be the subject of withholding tax will be rents, royalties, etc., which were in the law before. This section had to be rewritten to remove the provision for withholding tax on copyrights.

The CHAIRMAN: Shall subsection 2 carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Shall subsection 3 carry?

Some Hon. SENATORS: Carried.

The CHAIRMAN: Next we come to subsection 4.

Dr. EATON: That is putting back in the law what was there before. The only tax is a 10 per cent tax on motion picture films. The rest of the copyright is out. In repealing the copyright provision we had to re-enact the provision relating to motion picture films. There is no change in the law insofar as motion picture films are concerned.

Hon. Mr. HAYDEN: It is a 10 per cent withholding?

Mr. GAVSIE: Yes. There is no change in that.

Subsection (4) was agreed to.

The CHAIRMAN: The next is subsection (5), dealing with dividends, etc.

Dr. EATON: That deals with a very technical situation. I mentioned it a while ago in discussing an amendment relating to a company that claimed to be a non-resident company even though it was making loans of $500 or more in Canada. We corrected that situation. There was a provision in the law that the 5 per cent rate, the parent-subsidiary rate, could not be enjoyed by a company if more than 25 per cent of its income was from interest and dividends other than interest and dividends from a wholly-owned subsidiary. So a company which was actually carrying on the loan business was unable, through that exclusion, to get the 5 per cent rate on parent-subsidiary dividends, when it seemed quite right that they should, the same as any other company carrying on business in Canada. The amendment here is to say that that exclusion relating to income in the form of interest shall not apply to a company whose chief business is the making of loans and earning of interest.

Hon. Mr. HAYDEN: You have extended the law.

Dr. EATON: Yes. It is beneficial.

Hon. Mr. HORNER: That may be a lending company or insurance company?

Mr. GAVSIE: A lending company.

Dr. EATON: The main income of an insurance company would be premium income rather than interest income.

Subsection (5) was agreed to.

The CHAIRMAN: Subsection (6) (4), exemptions.

Dr. EATON: This is a provision whereby trust income may go out of Canada tax free. The general law is that payments by a trustee or an estate to a non-resident person are taxable 15 per cent. There is one exemption at present, namely, the income of or from a trust if it may reasonably be regarded as having been derived from dividends or interest received by the trustee from a non-resident owned investment corporation. We add to that provision the same right in respect of copyright royalties that may flow through the trustee and be received by the non-resident free of tax.

Hon. Mr. LAMBERT: What is the opinion of the Foreign Exchange Control Board on that?

Dr. EATON: It has no objection.

Hon. Mr. MCDONALD: Mr. Chairman, will you excuse a personal reference for the purpose of a question? I am a trustee, and when I get the quarterly dividend cheque I have to take it to the bank and have the 15 per cent deducted and have the bank send their cheque on. Could not the head office of the bank make the deduction and save me that trouble?

Hon. Mr. HAYDEN: In this case there is no tax.

The CHAIRMAN: Is that from a non-resident corporation?

Hon. Mr. MCDONALD: It is from the Royal Bank, going to a non-resident.

Mr. GAVSIE: The money is passed on to you, senator, as the Canadian resident trustee, and if you remit any of the funds outside you are obliged to make the withholding.

Subsection (6) (4), was agreed to.

The CHAIRMAN: Subsection (6) (5), trust beneficiaries residing outside of Canada.

Dr. EATON: This is a beneficial amendment and it has a very narrow application. The provision is that where the source of income of the trustee is, for example, entirely in the United States, and if the payment is to a resident of that country which is the source of the income, there will be no 15 per cent tax on the payment by the trustee to the non-resident beneficiary, if the trust was set up before a certain date.

Hon. Mr. HAYDEN: You mean if the trust funds are received from securities outside of Canada and the beneficiary is outside of Canada—

Dr. EATON: In the same country.

Hon. Mr. HAYDEN: Then the trustee in Canada can bring them in and complete the circle without withholding any tax?

Dr. EATON: Yes.

Hon. Mr. HORNER: Do you mean that a person outside of Canada has a preferred position to one in Canada?

Hon. Mr. HAYDEN: No. This applies where the securities and earnings and beneficiaries are outside of Canada but the trustee administering them is in Canada.

The CHAIRMAN: And the income would probably be taxable in the United States.

Subsection (6) (5) was agreed to.

Subsection 7, application of section was agreed to.

On section 39—redemption by non-resident owned corporation.

Dr. EATON: The underlined words at the bottom of the page, "the corporation's surplus determined in a prescribed manner," are new. The wording of the present subsection is shown in the explanatory note on the opposite page. The new wording enables the department to be more lenient in saying what shall be deemed to be distributable income.

Hon. Mr. HAYDEN: This says "the payment made shall, for the purpose of this part, be deemed to be the payment of a dividend . . ." A dividend is not taxable once the non-resident owned corporation has paid the 15 per cent tax.

Dr. EATON: This does not relate to a non-resident owned corporation.

Hon. Mr. HAYDEN: It does, according to the wording.

Dr. EATON: It is not technically what you and I mean by a non-resident owned corporation, is it?

Hon. Mr. HAYDEN: The marginal note reads, "Redemption by non-resident owned corporation."

Dr. EATON: My mistake, that is correct.

The CHAIRMAN: Section 96 deals with non-resident persons, and section 39 of the bill purports to amend subsections 2 and 3 of section 97; section 97 in turn relates back to section 96. To that extent it must apply to non-residents.

Mr. GAVSIE: Under the old wording it was found that if the equivalent tax had not been paid by 1932, where the corporation had elected to be taxed as an N.R.O. corporation, it could never get the benefit of exemption from a non-resident holding. This provides for the calculation of what its income was at that time, in accordance with the regulations.

Dr. EATON: It is really the same thing, that is the whole income before taxation.

Hon. Mr. HAYDEN: It is not puzzling to me. I merely point out that you say it shall be deemed to be the same as dividends; and all I say is that the ordinary incidence attached to the dividends of N.R.O. corporations is that they are not taxable.

Dr. EATON: That is all right.

Section 39 (1) was agreed to.

The CHAIRMAN: We are now on subsection 2 of section 39.

Dr. EATON: That arises out of the position of non-resident insurance companies, carrying on business in Canada. There is a long story behind that and I am not sure that I can shorten it very much. The insurance companies are in a dual position, that of carrying on business in Canada and being non-resident. The problem arises as to how their investment portfolio, even their head office portfolio, shall be treated for the purpose of non-resident tax. Up until the time this law came into force there were two taxes. They had interest and dividends received at a premium, with a five per cent tax on residents, applied to everybody; and, an added tax of 15 per cent on non-residents. The problem of this dual position, and being subject to two taxes, came up. They pointed out that it was not fair that they should pay both taxes. Under the power of the Minister, under the old Act, they were deemed to be residents, and as such were freed entirely from the 15 per cent tax on non-residents. They were, however, liable to the 5 per cent tax in respect of interest and dividends received as premiums applicable to residents of Canada. When the new income tax was introduced, the 5 per cent tax on interest and dividends received at a premium was repealed, and the insurance companies were in the position of having no tax at all to pay under these two sections. In the meantime we are

trying to work out a satisfactory formula for taxing them as non-residents to a limited extent. The formula is being discussed with them, but has not yet been worked out.

Hon. Mr. HAYDEN: This is enabling legislation?

Dr. EATON: Yes, enabling legislation, to abate the full force of the 15 per cent tax on insurance companies, mainly due to the fact that because of their business they are required to hold certain Canadian securities. We are trying to work out a satisfactory formula.

Hon. Mr. HAYDEN: You are working with them.

Dr. EATON: That is correct.

Hon. Mr. NICOL: How do you tax reciprocals?

Mr. GAVSIE: Only on the general reserves, in the same way as we do the mutuals and co-operatives, if part of the income is deemed to be a general reserve. I guess that is putting it rather bluntly.

Hon. Mr. HAYDEN: Yes.

Hon. Mr. NICOL: How do you tax the insurance companies who do a very large business here?

Mr. GAVSIE: You see, sir, they only became taxable in 1947, and I do not think the assessments have been finalized. We have been discussing it with them, and a method of taxation is being worked out, though I cannot give you the definite answer as to how we are taxing them. We have been in conversation with the Department of Insurance for quite a while, and I think we have a method worked out.

Hon. Mr. NICOL: With respect to the local corporations, I think you have worked out a scheme which is satisfactory. I would point out that practically four-fifths of the business is foreign business, that is with either English or American companies, and, as far as I know most of these foreign companies are not paying the taxes which are being paid by the local companies.

Hon. Mr. HAYDEN: The mutual companies only became taxable as of January 1, 1947, following the Royal Commission.

Hon. Mr. NICOL: I am speaking of reciprocals, and particularly the New England companies. Those companies came here, secured licenses from the different provinces, but did not pay the taxes that Canadian companies were paying.

Hon. Mr. HAYDEN: But they were not subject to any tax under the law until 1947.

Hon. Mr. NICOL: We are making the law.

Hon. Mr. HAYDEN: We made the law effective January 1, 1947.

Hon. Mr. NICOL: But we are making the law now.

Hon. Mr. HAYDEN: Not any more.

Hon. Mr. NICOL: I understand that these foreign companies do not pay taxes equivalent to those paid by Canadian companies.

Mr. GAVSIE: They will pay taxes on what is regarded as their income, but as the industrial factory mutuals operate, they get a payment which I understand is in the nature of a deposit and it is only taken out as used. We are now working out the part that will be regarded as their income, and they will be taxed on that.

Hon. Mr. NICOL: But you are not doing it at the present?

Mr. GAVSIE: Yes, since 1947.

Hon. Mr. HAYDEN: Since and including 1947.

Mr. GAVSIE: I do not want to make any suggestions as to whether or not they are being taxed enough. That is not my function. Parliament in 1947 provided for their taxation, and we have taken it up with them; we have indicated to them what we regard as their income, which is subject to taxation under the law.

Hon. Mr. NICOL: Are the reciprocals paying any taxation on their profits?

Mr. GAVSIE: They will be taxed.

Hon. Mr. NICOL: I am not concerned with whether they will be, but are they being taxed on their profits?

Mr. GAVSIE: I think the answer is "yes".

Hon. Mr. NICOL: If they are not making profits they return money to their policyholders.

Mr. GAVSIE: I cannot answer that. I have taken an oath of secrecy, but in this case I can speak freely and say that I do not know whether they are making a profit; but, certainly, if they have an income they will be taxed in accordance with the law. They are subject to tax, and we are proceeding to assess them.

Hon. Mr. HUGESSEN: But this section—

Mr. GAVSIE: It has nothing to do with it. The provision for taxing them is found in the Act itself. All this section does is deal with the non-residents, and refers particularly to life companies. They have a portfolio in Canada now; technically, they should be subject to withholding taxes on all their interest and dividends from that portfolio in Canada, but there is a certain part of that portfolio which is maintained in Canada. They are required by the Insurance Act to have sufficient securities to cover their liabilities in Canada, and what is now being discussed with the life companies is a procedure whereby the portfolio that relates to their liabilities in Canada might be relieved of the 15 per cent tax. This is just enabling legislation, and when the formula is worked out it will go into legal effect.

Hon. Mr. NICOL: Have the reciprocals any deposit with the department?

Mr. GAVSIE: Not with our department, but I believe they have with the Insurance Department.

Hon. Mr. HAYDEN: They must have.

Hon. Mr. NICOL: They have no capital.

Subsections (2) and (3) were agreed to.

The section was agreed to.

On section 40—deduction.

Mr. GAVSIE: That is exactly the same thing. That is part of what we have been discussing. If we work out this arrangement we would have to make some arrangement providing for the insurance companies making a return of the amount of their income, and paying the tax.

The section was agreed to.

On section 41—optional method of payment.

Mr. GAVSIE: There is a provision in the Act that in the case of a non-resident holding real estate in Canada there is a 15 per cent withholding tax on the gross. There is also a provision in the Act that non-residents can file on a net basis. This is a provision to allow of the operation of an optional method as far as withholding is concerned pending the filing of the return on the net basis. Under the law as it exists at the present time the agent has no alternative but to withhold the 15 per cent on the gross and remit it to the department, and when the non-resident files on a net basis, to apply for a refund. This sets up a method whereby the agent, if he files an undertaking from the non-resident to file the

return, the agent being personally responsible, can, instead of deducting on the gross, deduct on the net and remit it to the department. But if the non-resident subsequently fails to carry out his undertaking the agent will be personally responsible. That is the chance he takes if he wants to take this election.

Hon. Mr. HAYDEN: It is beneficial.

The section was agreed to.

On section 42—administration of oaths.

The CHAIRMAN: This section deals with the administration of oaths.

Mr. GAVSIE: I am told that this provision is in other Dominion statutes, such as unemployment insurance. The minister may authorize officers of the department to take the oaths, rather than go say to the Superior Court and have a commission issued.

The section was agreed to.

On section 43—French version amended.

Mr. GAVSIE: This is a correction in the French version of the Act. It appears in the first line. The sense of the old Act was that if a person gives a release to a party after we have issued a so-called letter of garnishment—what it really meant was, if he pays his debt after he gets this letter he is still personally liable. In other words, having got the letter of garnishment from the department he cannot discharge his debt. The French version said that he grants a discharge when it really means that he discharges his obligation by paying. It is to correct the French version.

The section was agreed to.

On section 44—withholding taxes.

Mr. GAVSIE: The first part is made necessary because of the new Bankruptcy Act containing the priority or privilege, so we are now removing the reference to the Bankruptcy Act.

Subsection (1) was agreed to.

Mr. GAVSIE: Subsection (2) is to correct in inadvertent change that was made in the new act as compared to the old bill. It provided for a penalty on failure to remit the withholding tax. It provided a penalty of the amount of the tax, whereas in the case of a resident it should only be a percentage. That has been the penalty; and this puts it in line with the way it was under the Income War Tax Act.

The CHAIRMAN: This limits it to 10 per cent?

Mr. GAVSIE: That is right.

Subsections (2) and (3) agreed to.

The section was agreed to.

On section 45—"corporation" and "corporation incorporated in Canada".

The CHAIRMAN: This seems to deal with certain definitions.

Mr. GAVSIE: Yes, amendments to the definitions.

The CHAIRMAN: Which are contained in section 127 of the Income Tax Act.

Mr. GAVSIE: The amendment is required, since Newfoundland has come into Confederation, to make sure that "corporation" includes a corporation incorporated in any part of Canada before or after it became part of Canada.

Subsection (1) agreed to.

On subsection (2):

Dr. EATON: This is part of that amendment we spoke of some time ago, whereby Canadian holders of United States Steel and Chrysler, etc., would not be taxable in respect of capitalization or stock dividends declared or paid by a United States corporation.

Hon. Mr. NICOL: Does that apply only to those corporations?

Dr. EATON: No, sir. It applies to any corporation more than 50 per cent of whose shares are held by non-residents.

Hon. Mr. HORNER: It says here "where the stock dividend has been declared by a non-resident corporation, more than 50 per cent of the share capital of which (having full voting rights under all circumstances) belongs to non-resident persons". What is the meaning of the clause?

Dr. EATON: This, that non-residents control the policy of the company, and in declaring stock dividends or capitalizing, Canadian companies have to be very careful of that, or they will bring on a terrific tax liability on their shoulders through capitalization of undistributed income on hand; and it seemed somewhat unfair that a corporation over which Canadians have no control could, for reasons of their own, quite apart from any tax question, go ahead and act and inadvertently bring on a terrific tax liability on Canadian shareholders.

Mr. GAVSIE: The "non-resident persons" are Canadians. In other words, they are non-residents, compared with the "non-resident corporation", which is in the United States. Those are Canadian shareholders receiving a stock dividend from an American corporation and not subject to tax. The benefit is to the Canadians.

Subsection (2) was agreed to.

Mr. GAVSIE: Subsection (3) is just to take out "or 28".

The CHAIRMAN: Technical.

The subsection was agreed to.

The CHAIRMAN: Subsection (4) relates to the definition of "loss". Here again it is a technical change to omit the words "or 28".

The subsection was agreed to.

Dr. EATON: The effect of subsection (5) is to take directors' fees out from under the investment tax of 4 per cent.

Hon. Mr. HAYDEN: It is part of general income?

Dr. EATON: That is correct.

Hon. Mr. HUGESSEN: To treat them as earned income?

Dr. EATON: Yes.

Mr. GAVSIE: Subsection (6) is amended for exactly the same reason.

The subsection was agreed to.

The CHAIRMAN: Subsection (7) deals with the definition of "taxation year".

Dr. EATON: There is an ambiguity in the present law, where a company changes its fiscal year, and where it does, it has two fiscal periods ending in one year, on the question of what constitutes a taxation year for purposes of taxation, purposes of the law. It is amended so that any fiscal period ending in the year is a fiscal year.

The subsection was agreed to.

The section was agreed to.

On section 46—investigation, etcetera.

The CHAIRMAN: This section deals with the repeal of subsection (10) of section 129 and substitutes a new subsection therefor.

Mr. GAVSIE: The purpose of this is that the collection procedure and the enforcement procedure that are applicable to the new act will be applicable to outstanding accounts under the old act. The position we are in now is, to take the taxpayer who owes taxes for 1945, 1946, 1948, 1949 and 1950, to have two procedures running against him when we have to take collection action.

Hon. Mr. HAYDEN: It covers more than collection.

Mr. GAVSIE: Well, that is the first thing. Sections 108 and 109 deal with investigation procedure.

Hon. Mr. HAYDEN: It covers search and inquiry.

Mr. GAVSIE: I am sorry, sections 108 and 109 are the collection procedures and 110 deals with the seizure of chattels, which as far as I am aware has never been used. Section 115 is the investigation procedure.

Hon. Mr. HAYDEN: The investigation procedure as provided in the new Act would apply from this date in respect to past years.

Mr. GAVSIE: Yes, and so we would have one system. This is purely procedural in order to have one system rather than operating two at the same time.

The CHAIRMAN: Shall section 46 carry?

Some Hon. SENATORS: Carried.

On section 47—foreign tax deduction under Income War Tax and Excise Profits Tax Acts.

Hon. Mr. HAYDEN: There is no use repeating what I said about section 32 (3) earlier today about declaring what the law always has been, but perhaps the officers would explain this. This has been enforced for years and it is up to the courts to settle the matter. Maybe it is not a large matter.

Dr. EATON: As far as I know there are four or five companies involved in this.

Hon. Mr. NICOL: Are there any cases pending?

Dr. EATON: So far as I know there were no appeals with respect to this provision when this Act was given first reading in the House of Commons.

Hon. Mr. NICOL: Have some cases come up since?

Dr. EATON: I believe there has been an appeal since this bill was given first reading.

Hon. Mr. NICOL: Is it the same case to which you referred a while ago?

Hon. Mr. HAYDEN: No, it is an entirely different matter.

Hon. Mr. DUTREMBLAY: Does this apply only in excess profits?

Hon. Mr. HAYDEN: No.

Mr. GAVSIE: I understand this was amended in the House of Commons so as to be limited to a much greater extent than it was in the bill. All it applies to now is what you call a 4 (R) dividend that comes into Canada tax free, and is not included in the income of the parent company. It is a dividend from a subsidiary that comes into Canada tax free. It is not included for tax purposes whatsoever. Now, if it comes from the United States, that country withholds 15 per cent of that dividend. This is to make it clear, that since Canada does not in any way tax them, there is no tax credit given in respect to that dividend.

Hon. Mr. HAYDEN: Then, you are not working any hardship.

Mr. GAVSIE: Oh, no.

Hon. Mr. HAYDEN: They would be getting an unfair advantage if you permitted the other possible interpretation.

Mr. GAVSIE: There is no question about that.

Dr. EATON: The tax credits were to remove double taxation, but now we do not tax these dividends so therefore there should be no tax credit.

Hon. Mr. HAYDEN: With that explanation it is not so bad.

Section 47 was agreed to.

On section 48—Newfoundland.

The CHAIRMAN: This section deals with some special rules relating to the province of Newfoundland, or to a taxpayer who was a resident in Newfoundland on March 31, 1949.

Hon. Mr. HAYDEN: Is this just what you would call transitional?

Mr. GAVSIE: It implements the terms of the union.

Hon. Mr. HAYDEN: After they get over the hump that this takes care of, then they are in the regular tax stream.

Mr. GAVSIE: That is right.

The CHAIRMAN: Gentlemen, are you prepared to deal with section 48 as a whole, including subsection 1 to subsection 8?

Some Hon. SENATORS: Carried.

Section 48 was agreed to.

On section 49—pre-confederation tax exemptions.

The CHAIRMAN: This section is to carry out paragraph 15 of the resolution, which reads as follows:

> That tax concessions under statutes of Newfoundland shall not apply in respect of taxes imposed by any act of the parliament of Canada.

Some Hon. SENATORS: Carried.

Hon. Mr. McLEAN: No one here is representing Newfoundland, so surely some of us should take time to read this over.

Hon. Mr. HAYDEN: I have read it over several times, and I think it is a proper section.

Hon. Mr. BEAUBIEN: We are all representing Newfoundland.

Hon. Mr. CAMPBELL: Was this provision contained in the treaty?

Hon. Mr. McLEAN: It is not right to pass in ten seconds something that may not be good legislation.

Hon. Mr. CAMPBELL: Can you say whether this provision was contained in the treaty signed by Canada and Newfoundland, whereby they agreed to waive any tax concessions they had at the time Newfoundland entered Confederation?

Mr. GAVSIE: You mean the terms of the union?

Hon. Mr. CAMPBELL: Yes.

Mr. GAVSIE: I think so.

Hon. Mr. CAMPBELL: Then this is just to implement the terms of the union?

Mr. GAVSIE: Yes.

Hon. Mr. HAYDEN: The explanatory note on the opposite side of the page refers to paragraph 15 of the resolution. What is that?

Mr. GAVSIE: That was the budget resolution.

The CHAIRMAN: I think it is well known that this has some bearing on certain tax arrangements which were made by the government of Newfoundland prior to Confederation, and which were not perpetuated in so far as the government of Canada is concerned after Confederation.

Hon. Mr. HAYDEN: And the provision that was in this section was incorporated in the budget resolution in March of this year.

The CHAIRMAN: That is correct.

Dr. EATON: And again in October.

Hon. Mr. HAYDEN: Yes.

Hon. Mr. McLEAN: Before this bill was finally put into shape one of the representatives of Newfoundland passed away and the other two have gone home. I think we should read it very carefully.

The CHAIRMAN: Are there any other questions in respect to section 49?

Hon. Mr. MACLENNAN: As I understand it the Honourable Senator McLean is saying that nobody here is representing Newfoundland. I do not think he is correct in that.

The CHAIRMAN: I think every person sitting around this table feels that he is representing the province of Newfoundland just as much as he is representing any other province.

Hon. Mr. MCLENNAN: Yes.

Hon. Mr. MCLEAN: It mentions Newfoundland several times.

The CHAIRMAN: This particular section relates particularly to the province of Newfoundland.

Dr. EATON: It states that any tax exemptions granted by Newfoundland shall not apply in respect of taxes imposed by the parliament of Canada. That is, concessions made by Newfoundland are not binding on the government of Canada.

Hon. Mr. HORNER: That is, any concessions made prior to March 31, 1949?

The CHAIRMAN: The significance of that date, Senator Horner, is that that is the last day preceding confederation.

Hon. Mr. HORNER: So that this law cannot reach back before the time of Newfoundland's entry into union with Canada.

Hon. Mr. MCLEAN: Certainly it does reach back, because it cancels any arrangements made by Newfoundland.

Hon. Mr. ROEBUCK: What arrangements did Newfoundland make? What arrangements are abolished by this provision?

Hon. Mr. MCLEAN: When Newfoundland was an autonomous country its government made certain arrangements with companies, and this provision nullifies those arrangements.

Dr. EATON: It does not nullify them; it simply says that they do not bind the government of Canada?

Hon. Mr. MCLEAN: Well, that nullifies them. I am not against the provision, but I think we should understand what it means. When Newfoundland was an autonomous country its government made certain income tax arrangements and this section brings all such arrangements to an end.

The CHAIRMAN: It may not bring them to an end.

Hon. Mr. MCLEAN: Well, the courts will decide that.

The CHAIRMAN: The provision means that they will have no effect under this Income Tax Act.

Section 49 was agreed to.

On section 50.

Dr. EATON: Section 50 makes provision for authority to continue any concession which is made by international agreement.

Hon. Mr. HAYDEN: That may be beneficial to Newfoundland.

Section 50 was agreed to.

On section 51—refunds.

Mr. GAVSIE: That is a beneficial provision, in that the small taxpayer who worked during the war and had some amount witheld from his salary is required under the present law to apply for a refund within two years, and this permits the minister to make a refund even though two years have expired. In some cases a tax deduction may have been paid from the salary even though the individual was not taxable in the year or years in question.

Section 51 was agreed to.

On section 52—Income Tax Appeal Board and Exchequer Court Appeals.

Dr. EATON: The purpose of this section is to make it clear that we have one Income Tax Appeal Board. It will be remembered that the Income War Tax Act provided for a Tax Appeal Board, and that the new act passed last year also provided for a Tax Appeal Board.

Hon. Mr. HAYDEN: I raised the point last year that this provision should be in the act, but the minister said it was not necessary. There must have been a change of mind.

Mr. GAVSIE: We get wise after the event. The government did not see fit to pay two sets of salaries.

Hon. Mr. NICOL: What happens to any cases that were pending before the other board?

Mr. GAVSIE: They will be taken care of. We are not affecting any rights at all; the section simply consolidates the Appeal Boards. The provisions for appeal are not affected in any way, but all appeals will be made to the one board. The board deals only with assessments from 1946 on.

Section 52 was agreed to.

On section 53 (1), —deductions from income of corporations in petroleum business.

Dr. EATON: This section is the renewal of the write-off concessions to mining and oil companies with respect to exploration and development expenses.

Hon. Mr. HORNER: This provides a tax concession to oil men?

Dr. EATON: That is right.

Hon. Mr. HORNER: Is it new?

Dr. EATON: No sir. The provision was first enacted during wartime to encourage production of strategic materials and it has been renewed annually ever since.

Hon. Mr. HAYDEN: This is prospective to and including the year 1952.

Dr. EATON: That is so. The companies complained that renewal for a year only did not give them time to plan their programs.

Hon. Mr. HAYDEN: This is very necessary, having regard to our mining and oil development.

Dr. EATON: It may be.

Subsections (1) to (7) inclusive, of section 53 were agreed to.

On subsection (8)—expenses deductible.

Hon. Mr. PATERSON: What is the effect of this, Mr. Chairman?

Hon. Mr. HAYDEN: It entitles mining and oil companies to charge off expenses incurred directly or indirectly in searching for minerals.

Dr. EATON: And it does not matter whether the mine or oil well is successful or not. Briefly, the position used to be this. If a mine was discovered or an oil well came in there was income created against which pre-production expenses could be charged. If, however, the exploration was off property and was unsuccessful that is regarded as a capital expenditure not related to the earning of any particular income, and is disallowed. This section, in effect, says no matter where you explore off property the exploration expenses in any development work done in any part of Canada can be taken into account and charged to profits.

Hon. Mr. PATERSON: All in one year?

Dr. EATON: If the profits are not large enough to absorb all the expenses in one year, they may be carried forward.

Hon. Mr. NICOL: If a successful mining company has large enough surpluses, which would be liable to taxation, it could decide instead of paying taxes to charter airplanes and go away on exploration expeditions.

Hon. Mr. LAMBERT: Re-investment.

Hon. Mr. NICOL: That is deductible?

Dr. EATON: That is correct; that is deducted before taxation.

Hon. Mr. NICOL: Then some of us may take some trips?

The CHAIRMAN: You must first have a successful mining property.

Hon. Mr. PATERSON: Mr. Chairman, some of the operators up in the Labrador may spend money for ten years before making a dollar. Are they going to charge all those expenses up when they do start to make money?

The CHAIRMAN: This only goes up to 1952.

Section 53 was agreed to.

Hon. Mr. HAYDEN: Mr. Chairman, might we revert for a moment to section 13, at page 13 of the bill? I think it is obvious that something has been left out of the section. You will notice that it says:

> Where an individual was resident in Canada during part of a taxation year, and during some other part of the year was not resident in Canada, was not employed in Canada and was not carrying on business in Canada, for the purpose of this Act, his taxable income for the taxation year is
>
> (*a*) his income for the period or periods in the year during which he was resident in Canada—

After the words "where an individual was resident in Canada during part of a taxation year . . . " there should be added "was employed in Canada or was carrying on business in Canada during part of the taxation year." Should not that be added to make sense?

Mr. GAVSIE: No, he may be doing one of three things.

Hon. Mr. HAYDEN: That is what you say. You start out by saying that he was a resident in Canada during part of the year, and in another part of the year he was not resident in Canada and not doing business in Canada; then you are going to charge him taxation for part of the year when he was employed in Canada.

The CHAIRMAN: It is a question of how you read that section. It is a question whether the words "and during some other part of the year was not resident in Canada . . . " govern everything that follows.

Hon. Mr. HAYDEN: Actually, I think that is what is intended.

Mr. GAVSIE: In order for him to be taxed on income for part of the year, he must have been resident in Canada only for part of the year and not employed or engaged in business. In other words, a man may be a resident in Canada for part of the year; he may leave Canada and take up residence outside the country, but continue to carry on business in Canada.

Hon. Mr. HAYDEN: But you say in paragraph (*a*) "his income for the period or periods in the year during which he was resident in Canada, was employed in Canada or was carrying on business in Canada . . . "

Mr. GAVSIE: In order for this section to operate he must first be a resident in Canada during part of the year and outside Canada for another part of the year, and not employed in Canada or not carrying on business in Canada. If either of those other features apply then the section is inapplicable to him. That is what is intended, and that is the way it reads.

Hon. Mr. HAYDEN: Very well, if you want confusion, far be it from me to interfere.

Hon. Mr. DuTremblay: Under clause 7, at page 6, I understand that in the case of an expropriation it is equal to a sale.

Mr. Gavsie: That is correct.

Hon. Mr. DuTremblay: What proportion of the two or three years will be allowed?

Mr. Gavsie: There would be the part that represents the reimbursement of depreciation after the capital profit is taken out.

Hon. Mr. DuTremblay: Would it be for only those two or three years from 1949?

Mr. Gavsie: Yes; we do not go behind 1949.

Hon. Mr. DuTremblay: What proportion would be charged?

Hon. Mr. Hayden: According to the amount you had charged off for depreciation.

Mr. Gavsie: It would be the balance to be depreciated, which would neutralize itself; and the recapture would apply to any amount that you may have written off by way of capital allowance since 1949. That is the amount that would be concerned here.

Hon. Mr. Hayden: There is another question. Suppose in the case of a bond issue on a property when disposition is made of the property the proceeds must be paid to a trustee. That would mean that the entire proceeds would have to go to the trustee, and the company would have to pay an additional tax on the amount of recaptured depreciation.

Mr. Gavsie: I do not think the amount going to the trustee would exceed the amount remaining to be depreciated.

Hon. Mr. Hayden: I am referring to the entire amount of expropriation, if there was a bond issue.

Mr. Gavsie: But I do not think that the amount to go to the trustee would be any more than the amount necessary to redeem the bonds, and the depreciation that the company would have taken would have some relation to the sinking fund for the redemption of the bonds.

The title was agreed to.

The bill was carried.

The Chairman: Shall I report the bill without any amendment?

Some Hon. Senators: Carried.

At 9.15 p.m. the committee adjourned.